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H.R. 962, THE ECONOMIC GROWTH AND FINANCIAL INSTITUTIONS REGULATORY PAPERWORK REDUCTION ACT OF 1993

THURSDAY, SEPTEMBER 23, 1993

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
SUPERVISION, REGULATION AND DEPOSIT INSURANCE,
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:30 a.m., in room 2128, Rayburn House Office Building, Hon. Stephen L. Neal [chairman of the subcommittee] presiding.

Present: Chairman Neal, Representatives Flake, Orton, Bacchus, Klein, Maloney, Barrett, McCollum, Pryce, Grams, and Huffington.

Chairman NEAL. I would like to call the subcommittee to order at this time. And I would like to welcome everyone to today's hearing on regulatory reform and credit availability, and on H.R. 962, the bill dealing with this issue that has been introduced by Mr. Bereuter and Mr. Bacchus.

Last week we heard from representatives of banking and consumer groups. All agree on the broad goals that regulation should be more effective, less costly, less burdensome, while assuring a safe and sound banking system, bringing credit available to all creditworthy borrowers. I believe these principles must guide us as we examine our system for regulating financial institutions in this country.

Last night, President Clinton spoke on health care. For one of the points he made in support of simplifying the system, he told how doctors at one hospital spend so much time filling out forms that they can see 200 fewer patients a year. He told how one hospital administrator spends $200 million a year on paperwork that has nothing to do with treating patients.

Our banking system is headed in the same direction. Bankers are spending more and more time filling out reports, studying new regulations, and worrying about required paperwork than they are in tending to their business of making loans. Something has to be done to get the spiraling burden of paperwork under control in banking as well as in health care and I am sure other industries as well.

One fact stands out. The more time bankers must spend figuring out regulations and figuring out forms, the less they can spend on making loans. And the more money they must spend to comply with Federal laws, the less they have to lend.

As I indicated last week, the administration has taken important steps on this issue with its regulatory proposals addressing credit availability, with efforts to ease loan documentation and appraisal requirements, among others.

I also applaud the administration's current effort to make the Community Reinvestment Act more workable. Congress also needs to act on this issue because it is our responsibility as lawmakers to review the current banking laws and make needed changes.

Our goal in pursuing regulatory reform must be to increase credit availability as much as possible while still maintaining strong safety and soundness protections.

Earlier this week the Senate Banking Committee acted on a community development bill which also contained regulatory reform, and secondary market for small business loan provisions. These are important pieces of the credit availability puzzle, and we should take note of the Senate approach of treating these items together.

The witnesses on today's first panel will tell us what is the view from the frontlines. The panel consists of three bank compliance officers who must deal every day with the real work of keeping their banks in compliance with the laws Congress has enacted.

We will then hear from a State regulator who will tell us how Federal and State agencies try to work together.

Finally, we will receive testimony from the General Accounting Office, which has produced literally thousands of pages of reports on our bank regulatory system and how it works.

I look forward to hearing the testimony of all the witnesses and working with them and other interested parties and with our colleagues on both sides of the aisle to make progress on this important issue.

I thank our witnesses for being with us this morning. Before recognizing them, I would like to recognize our distinguished ranking minority Member, Mr. McCollum.

Mr. McCollum. Thank you very much, Mr. Chairman. I thank you for convening this morning's hearing and allowing us the opportunity to get into testimony concerning the tremendous burdens the national banking industry has today in the area of regulatory overregulation. I think that is what we have today.

H.R. 962 that Mr. Bereuter and Mr. Bacchus have introduced has over 260 cosponsors including nearly a majority of the members of the Banking Committee. I am pleased that we have begun this particular review process. I think that we can provide a means of reducing bank regulations which are redundant without jeopardizing financial institutions' safety and soundness.

I hope we move just as quickly to mark up legislation; if not mark it up directly in relationship to this particular bill, to do it in conjunction with some other legislation.

As you noted, the Senate Banking Committee did report a bill out that contained some of the provisions found in H.R. 962 just this past Tuesday. It is a good first step. I don't think that they did nearly enough. I believe that most of what is in H.R. 962, if not all of it, should become law. And I would hope that we would do a far greater detailed job of producing legislation in this respect than so far has been done in the Senate.

To get at the real problems of undue cost, we must take a closer look at some of the provisions such as the section repealing 132 of FDIC—FDICIA, I can't go over the acronyms here—a section which requires the regulators to set guidelines for a number of internal controls. This is also a section which all the regulatory agencies have found to be poorly drafted and not well thought out. That is just one example.

It is clear that Mr. Bereuter and Mr. Bacchus' bill, H.R. 962, does not in any way alter the supervisory provisions which became part of FDICIA, such as continued annual supervisory examinations for troubled institutions, continued annual audits for institutions subject to the requirement, additional authority to close or restrict the activities of troubled institutions, and the 1991 banks bill's strong supervisory sanctions.

Mr. Chairman, I look forward to working with you and other subcommittee members in seeking a remedy to the problem of bank regulatory burdens. This morning I particularly welcome these witnesses, and I apologize in advance for the fact that I will have to miss much of the testimony due to the fact that I am also senior ranking Member of another one in Judiciary which is having a critical hearing this morning on a matter of great concern. But I will be in and out, and I have looked at your testimony, and it is a very, very important part of the process that we establish a record that gives us the basis to move forward.

I thank you for coming, for taking the time.

Thank you, Mr. Chairman.

Chairman NEAL. Thank you, sir. Mr. Orton.

Mr. ORTON. Thank you, Mr. Chairman.

I would also like to echo what you and Mr. McCollum have said regarding this hearing, and thank the witnesses for coming and sharing their time and expertise with us. I would like to commend the chairman for holding this hearing.

I, too, am very committed to the principles and concept of regulatory reform. I have looked at what the Senate has done in their markup yesterday. I would agree with Mr. McCollum, these principles ought to be brought forward to give us an opportunity to debate and vote on them.

I think clearly the cosponsorship of H.R. 962 in the House shows that the will of the clear majority on both sides of the aisle is that we debate and adopt meaningful regular reform.

I am somewhat concerned that the full committee may either refuse to bring up this bill or refuse to allow amendments to be put on the Community Development Bank bill with regard to this. And that is a great concern, that we may not reflect the will of the majority of this body. It is for that reason I have chosen today to fully endorse H.R. 962, and become a cosponsor. I had not previously done so because of an effort to work within the committee to bring forth a committee action on this.

It is now clear to me that we are going to have to use any means possible to get this issue to the full committee. And I commend Chairman Neal for holding these hearings and would urge the chairman to hold a markup on this bill and allow us to move forward on it.

So thank you, Mr. Chairman.

Chairman NEAL. Thank you, sir. Mr. Grams?

Mr. GRAMS. Thank you, Mr. Chairman.

I also would like to thank you for holding this series of hearings on regulatory burden relief and H.R. 962, the Economic Growth and Financial Institutions Regulatory Paperwork Reduction Act, a long name.

I also would like to welcome our distinguished witnesses today, in particular Kate Barr from Riverside Bank in Minneapolis. I have had a chance to review your prepared testimony and strongly agree with your statements that H.R. 962 is an excellent start in rethinking banking regulation and which regulations are effective and needed and which are duplicative, overly complex, and even counterproductive.

As a cosponsor of this legislation, I also believe that H.R. 962 would go a long way in beginning to improve the business climate, both in Minnesota and across the Nation. Again, I want to thank the witnesses in advance for their important testimony today, and you, Mr. Chairman, for holding these hearings. I too have a number of other commitments this morning so I will be in and out of the hearing. But I have your testimony and I look forward to reading the others as well.

So again, thank you very much for coming, and welcome.

Thank you, Mr. Chairman.

Chairman NEAL. Thank you.

Now I would like to welcome our panel. Ms. Kate Barr, senior vice president, Riverside Bank, Minneapolis, Minnesota; Mr. Stephen A. Kase, general counsel, Bank of Sturgeon Bay, Sturgeon Bay, Wisconsin; Ms. Diane Lopez, senior vice president, First Interstate Bank of Texas.

Thank you all very much for coming this morning. We will put your entire statements in the record, and ask that you summarize them a bit so we have a little more time for questions and answers. If there is no objection, we will just hear from you in the order in which I mentioned your names, and so, again, thank you.

Ms. Barr, we will hear from you.

STATEMENT OF KATE BARR, SENIOR VICE PRESIDENT, RIVERSIDE BANK

Ms. BARR. Mr. Chairman, I appreciate the invitation to appear today and share the experience of a small commercial bank in dealing with bank regulations.

Riverside Bank is a $125 million bank located in Minneapolis, Minnesota, with three branch offices in addition to our main office. Since we are a small bank in the midst of many of our competitors, we have sought out a niche in the small business banking market. We have been successful in doing that with 65 percent of our $8 million loan portfolio in commercial loans to small businesses. Our loans range in size from $10,000 to $1 million, and in industry from retail and wholesale sales to manufacturing and service.

My responsibilities at Riverside include managing compliance with regulations as well as marketing, planning, and lending. We are a small bank.

My responsibilities have included regulatory compliance since 1982, but the scope of that responsibility has increased dramatically in the last 3 years, particularly with FIRREA and FDICIA. In addition to my efforts, we have staff people with responsibilities for many regulations. No one single regulation, of course, is responsible for the growth of regulatory compliance. But it is the cumulative effect of layers and overlapping layers of regulations issued by different agencies but over a short period of time.

The overall impact on Riverside Bank of increasing requirements has been increased costs for staff time, materials, training, and systems. We must even have additional personnel just to check over the compliance of the ones actually doing the work.

The need to add staff and other costs might not seem so onerous to us if each new provisions was clearly beneficial to either the bank or its customers. But unfortunately, that is not always the case. There has also been an impact on our customers, particularly borrowers.

Just a few years ago it was much simpler and less expensive to borrow money. Loan proposals that once took 2 days to approve and just a short time to transact now require additional documentation, including appraisals, environmental assessments, and many disclosures. Loan approvals take longer and significant out-of-pocket costs are borne by the small business borrowers.

These may also be the same customers who have worked with us for many years repaying many loans who now have to withstand this additional cost.

The Bacchus-Bereuter bill contains numerous provisions which will help to relieve some of the unnecessary burden of compliance. Each regulation and policy statement which has been adopted has its advocates with reason to believe that a problem needed correcting, and each has added another layer to the point of overwhelming small banks like mine.

None of the provisions of this bill individually will solve our dilemma but it does begin to peel away at the layers and it is an excellent start at rethinking bank regulation and determining which regulations are effective and which are not contributing.

I will address a few of the specific areas in the bill. The first is regulatory micromanagement. In the past 2 years, Riverside has adopted 12 new policies affecting lending investment management and deposits. Each policy was implemented after a new regulation or policy statement was issued by the FDIC.

Several of these 12 new policies replaced an existing policy, but with significant changes needed to comply with precise and detailed requirements. These new policies include real estate appraisals, branch closings, interbank liabilities, selection of securities dealers, and truth in savings.

I must admit we have been permitted to allow one policy to lapse in that period of time and that was highly leveraged loan transactions. The regulators discovered that banks were adequately monitoring their loan portfolio without this requirement.

Now, I cannot say these policies unilaterally are unnecessary and lacking in benefit, but many of them have been adopted only to satisfy regulatory requirements and include sections that have no application to a bank of our size.

The prudent real estate lending standards policy, for example, includes a description of how we would monitor and value a multiphase development project that we would never enter into. And the prudent investment strategies policy includes descriptions of mortgage-backed derivative products that we have never considered purchasing and which I don't even know—don't even understand.

Requiring banks to have written policies is wise. But it is not possible to mandate the details of these policies in a way that will be equally meaningful and beneficial to a $25 million bank and a $6 billion bank. Many factors influence the way banks are managed and each bank must be given the latitude to develop policies that benefit them in their own communities.

The examination process itself is very thorough and allows regulators to converse with bank management about their policies and prescribe changes if needed.

Policy mandates frequently require the bank to monitor the level of activity or volume of certain transactions such as loans over a certain loan-to-value ratio. We are seeing a trend toward artificial ceilings on activities based on aggregate totals with no regard for individual transactions.

We are particularly concerned at Riverside Bank about the effects of real estate lending standards. Because of our small size just a few sizable loans for community development projects could cause us to exceed the 30 percent of capital benchmark and cut off additional funds for these projects.

This is a good example of a rigid requirement that does not consider the ability of the bank's officers and directors to make well-considered lending decisions. All of the current policy requirements together, though, pale beside the prospect of section 132 of FDICIA, regarding standards of bank operating procedures.

If it is difficult to prescribe standards for real estate lending, it will be impossible to develop meaningful standards for operating procedures that will apply at every bank.

Banks are as much different from each other as they are the same. I appreciate the proposal in the bill to exempt well-capitalized and well-managed banks, but I do not think this will be effective for any bank.

It has been a time-consuming effort to keep up with the volume of new regulations and it has been especially difficult because of the frequently short time periods allowed.

For example, the policy on selecting securities dealers and prudent investment strategies had a 3-week implementation period and the policy on prudent real estate lending standards, which was a significant new policy, had an 8-week implementation period.

The short timeframes pressure us to rush the policy, while a longer preparation period would result in better policies because of the opportunity to consider all the options and their effects and explore the capabilities of our systems and operations.

I would like to speak to the issue of consumer inconvenience. There are several regulations in place that were enacted to provide consumers with information with which to make informed choices, but these regulations do not accomplish this goal and even may be counterproductive to it.

The worst example I am sure you have heard before is adjustable rate mortgage lending. An applicant for such a loan is subject to at least 10 separate disclosure provisions, each with their own mandated language, format, and timing requirements. We have procedures in place to comply but I doubt if the ultimate goal of consumer understanding is accomplished.

There are other examples in consumer mortgage lending of regulations which have been issued at different times and by different agencies which do not work together for the consumer's benefit.

Many banks of similar size to ours simply elect not to offer these kinds of products, especially adjustable rate mortgages and home equity lines. Because we are located in a large metropolitan area, we feel we cannot make that choice and remain competitive, so we therefore offer the product.

We recently purchased a software system for home equity lines at a cost of $4,000, yet we have a total of 166 of these loans. That is $24 per loan just for the disclosure. Recent changes to RSPA have expanded coverage for loans made for business purposes secured by real estate. We have already found that the disclosures serve no purpose except compliance for its own sake.

We recently made a loan for a business line of credit, for example, secured by guarantees of the two owners. Each owner secured their guarantee with mortgages on their homes which they owned free and clear. We were required under RSPA to provide them with early disclosures about transferring servicing rights and closing costs and with a settlement statement at closing which contained only two entries. RSPA is a valid regulation for consumer home mortgages and has no benefits for the business borrower.

The last title of the bill affects the Community Reinvestment Act. Riverside Bank is proud to have received outstanding CRA ratings in both 1992 and 1993. We believe this rating recognizes our active participation in community development and small business lending in Minneapolis.

Local government and media have both praised our willingness to go the extra mile to make projects work. These loans are not made because of CRA. We make them because they are good loans that are good for our community.

Unfortunately, I believe our outstanding rating might be more a reflection of our detailed documentation and computer reports. Our 12 calling officers have met with 52 different groups in the last year and completed 160 written reports to prove that they met with them.

We will spend $3,000 each year on computer-generated color maps to prove we make loans in Minneapolis. We will continue to spend time and other resources documenting our performance, lessening the time and resources available to actually perform. Any relief from this paperwork will enable us to dedicate these resources as they should be.

As a compliance professional, Mr. Chairman, I will continue to develop policies, procedures, and training necessary to comply with whatever regulations are implemented. But at the frontlines, we know that many of these regulations could be modified in such a way to lessen the burden while still achieving the ultimate goal of consumer protection and bank safety and soundness.

I do appreciate the invitation to appear today and share my experiences. Thank you.

[The prepared statement of Ms. Barr can be found in the appendix.]

Chairman NEAL. Thank you very much. Mr. Kase.

STATEMENT OF STEPHEN A. KASE, GENERAL COUNSEL, BANK OF STURGEON BAY

Mr. KASE. Thank you.

Mr. Chairman, the Bank of Sturgeon Bay is a 100-year-old community bank. It has grown to about $200 million in assets in a town of 10,000 people. It has done this essentially through hard work and local support and local effort. For 13 years I have served at my bank's compliance officer providing education, training, and implementation, both for banking regulation and numerous other laws which affect our operations.

I am honored to appear today to testify in support of H.R. 962. I do so with the distinct perspective of a small town rural community bank.

In the interests of time, I will summarize my written statement and limit comments to amendments of special significance to us. However, I welcome the opportunity to offer additional information as you feel appropriate.

As a nation we have a proud tradition of protecting those who cannot protect themselves. Banking regulation at its best adheres to this concept by maintaining the safety and soundness of financial institutions. It provides a level playing field for the consumer, assuring fair and equal access to banking services.

We strongly support regulatory supervision as a necessary part of banking. We do not dispute the need for safe and sound operation and consumer protection. We do our best to support our customers and our community. However, we constantly hear complaints about the interference of government regulation.

Our customers perceive that much of the cost in incomprehensibility and compliance simply appears unnecessary. This is where we become concerned about regulatory burden.

From our point of view, it means costly records and statistics, excessive penalties, and limited discretion to recognize good-faith compliance efforts. My bank tries to provide the widest possible range of credit products. However, we have been forced to limit products and service which might otherwise have been available. We do not offer adjustable rate mortgages. We cannot match deposit rate products with investments that do not incur similar regulations and restrictions.

I have an attached exhibit that demonstrates the cost of compliance for my bank. Although it may be considered simplistic, it offers hard facts about the increased time, paperwork, and cost of services caused by regulatory compliance.

It is best for me to focus on sections of particular importance to our bank. Hopefully, others will fill in the gaps, and in the end you will have a wide range of testimony from which to make your decisions.

First is section 122, Standards for Outside Directors. The amendment addresses the difference between the outside and the inside director. In the context of the community bank, we face a difficult challenge identifying women and men who are willing to serve.

The expectation of a sophisticated and experienced board of directors all fully knowledgeable about the operation of modern banking is unrealistic. Some directors become involved in management. Others participate based on a recognition of the need for community involvement.

Thus, the very goal served by regulations such as CRA places directors at high risk simply for their willingness to serve. We consider section 122 highly supportive of the community involvement without reducing the responsibility assessed upon those who willingly enter into the inner circle of bank management.

Sections 201 on Regulatory Standards, and 202, Paperwork Reduction Review. FDICIA certainly has focused on protecting financial institutions against failure. Unfortunately, institutions which were not troubled, which were well managed, were affected with massive rewriting of internal policies and procedures. It was not that they didn't deal with the issues, but that they simply did not address them in the manner now required by law.

This amendment recognizes that institutions already doing their job well do not need increased scrutiny created by the FDICIA-proposed standards. If the patient is examined and found healthy, what is the sense of prescribing expensive and unpleasant medicine?

The focus of corrective action should be on troubled institutions. These amendments will not reduce attention directed to those that need it, but relieve the burden imposed on those that don't.

Annual examinations in section 301 is among the most desirable elements in this legislation in the recognition of sound banks concerning regulatory examination. We must be prepared for examinations at our bank and holding company by both State and Federal regulators for safety and soundness and regulatory compliance, including CRA. This has resulted in as many as four distinct examinations within a single year.

Although conditions are essentially unchanged, both State and Federal regulators are required to separately evaluate the same concerns. The duplication of effort is obvious.

The amendment recognizes that if a bank demonstrates satisfactory performance, examination requirements can be adjusted accordingly. The cost savings is substantial, both to the bank and the regulatory agency.

At a time of almost insurmountable demands on the resources of government, section 301 would allow regulators to rely on the proved performance of successful banks and focus their attention where it is needed most.

Section 307, the Bank Secrecy Act. Although we take the act very seriously, the degree of accuracy required in BSA reporting and recordkeeping is intimidating. Fear of mistakes and its consequences sometimes overshadows the purposes of the act.

One change proposes to reduce unnecessary recording of nonreportable transactions by identified bank customers. A second allows for minor adjustments in cash reporting to match inflation.

The third transfers responsibility for cash transaction reporting from the bank to the customer.

Despite testimony to the contrary, I find nothing in these amendments that lessens the effectiveness of the act. Identification procedures are the same. Reporting and identification requirements remain intact. The significant change simply recognizes that it is the customer who provides the information rather than the innocent bank employee who is ultimately responsible for its accuracy.

Sections 406 for Disclosure and Equity Loans, and 442, Exemption of Business Loans from RSPA. RSPA was once a strongly supported regulation in our bank. It made sense and it was well intentioned. However, we now face a regulation which demands disclosure for lending efforts never intended by the original law.

The first amendment recognizes the merit of carefully crafted truth-in-lending disclosure for home equity loans. The concerns of RSPA are addressed by current disclosure. Duplication serves no purpose.

The second recognizes that business and agricultural lending involves borrowers who are better informed and educated. These changes only redirect RSPA toward its original purpose: To ensure that real people get real disclosure information when putting their homes at risk.

CRA amendments, section 501: I am a strong supporter of CRA and my bank, I am pleased to say, has also received two consecutive outstanding ratings. It recognizes the partnership of the bank and the community it serves. The regulation is straightforward and for many years caused no concern. The examination process only asked banks to show what they do, not do more than they should.

However, revised standards have created a regulatory nightmare. Banks are buried in a morass of useless paper and regulators struggle with problems of enforcement. Yet, consumer advocates assert the act has failed to do its job.

This amendment recognizes banks which pass the test, allows credit for lending initiatives, clarifies responsibilities for special purpose banks, and eliminates redundant examinations. These changes should not raise concerns. They reward banks that fulfill their responsibilities, provide guidelines for valid CRA initiatives, and reduce the duplication of efforts in States with equivalent laws.

These are not bad things. They do not undermine the purposes of the act. Rather, they only help to provide relief to banks seeking to comply with the law.

The problem of regulatory burden is as real as you could possibly imagine, and we need your help. I agree that banking regulation must be maintained and laws should not be changed without cause. However, this bill recognizes a critical need to balance the scales.

The amendments attempt to alleviate burdens for those banks that meet expectations and identify ways to reduce costs without sacrificing the safety or quality of our banking system. They reduce the dollar cost of compliance activity, reduce the complexity necessary for compliance, reduce penalties, and allow consumers more discretion, expand opportunities for lending, and they remove disincentives.

Congress faces a monumental task in overseeing the welfare of the country. In your deliberations, I urge you to recognize the importance of this bill to the banking industry.

For community banks, it is no longer a question of simply doing our job but of constantly proving we are doing it right. Every new obligation increases the complexity and cost of banking activity. No single piece of legislation makes or breaks the system, but at some point small community banks will no longer be able to cope.

Many have already decided it is easier to sell out, passing the burden on to regional or national banks better able to meet the awesome tasks of compliance. When that happens, we must question whether the consumer is better off without access to a locally owned and locally dedicated financial institution.

In closing, I sincerely commend the authors and collaborators and cosponsors of this bill for identifying numerous opportunities to improve banking regulation. It offers you the chance to recognize the effort and value of community banks like mine.

Seize this opportunity to support healthy and economically sound financial institutions. Help us to meet local credit needs and make banking services more affordable to the consumer.

Thank you.

[The prepared statement of Mr. Kase can be found in the appendix.]

Chairman NEAL. Thank you, sir.

Ms. Lopez.

STATEMENT OF DIANNE LOPEZ, SENIOR VICE PRESIDENT, FIRST INTERSTATE BANK OF TEXAS

Ms. LOPEZ. Mr. Chairman and members of the subcommittee, my name is Dianne Lopez. I am senior vice president and regional compliance manager of First Interstate Bank of Texas, N.A., Houston, Texas.

First Interstate Bank of Texas has 93 branches located throughout the State of Texas and has total assets of $5 billion. We are an affiliate of First Interstate Bancorp, a bank holding company owning 17 banks located in 13 States. First Interstate Bancorp is the 13th largest banking organization in the United States with total consolidated assets of $49.5 billion as of June 30, 1993. I am pleased to be here to testify on behalf of First Interstate and am testifying in favor of H.R. 962.

My testimony will focus on Titles 2, 4, and 5, since these sections will affect the regulations I work with on a daily basis.

Section 132 of FDICIA, the Federal Deposit Insurance Corporation Improvement Act, requires the bank regulatory agencies to set standards for internal controls and numerous other areas of a bank's day-to-day operations which affect asset quality. This micromanagement by the regulatory agencies is required by FDICIA regardless of a bank's capital or overall supervisory rating.

These stringent standards will strengthen the regulatory hold that has already been imposed by the savings and loan bailout bill, FIRREA, and could result in banks making fewer loans to new small businesses for fear of violating these rigorous controls on asset quality.

These controls should not apply to institutions that are adequately capitalized with a CAMEL rating of 1 or 2.

Title IV: Currently, the Truth in Lending Act requires an incredible amount of disclosure both at the time of application and upon each adjustment to the interest rate. I have brought samples of these disclosures for your review today. They are so onerous that this bank has not been able to operationally comply with the requirements since our conversion to a national bank charter in 1988, and therefore we did not offer this product to our customers until March of this year.

The ARM disclosures are so voluminous that they may in fact be confusing to the borrower. This bill would permit lenders to disclose either a history of the index to which the loan will be tied or a statement that the monthly payment may substantially increase or decrease over the life of the loan. The cap mandated by the Truth in Lending Act would still be applicable, and, of course, would be disclosed to the borrower, thus preventing a borrower from unknowingly entering into an adjustable rate mortgage that may eventually become unaffordable.

With respect to the Real Estate Settlement Procedures Act, this bill proposes to clarify that the truth-in-lending disclosures currently being provided to borrowers engaging in home equity and home improvement loans are not required to be duplicated by providing them again in the standard settlement form. This will not only ease the cost of compliance for these types of loans but will cause less confusion to the borrower.

Currently, under the Electronic Fund Transfer Act, a consumer's liability for unauthorized transfers is limited to $50 if the unauthorized transfers are reported within 2 days of discovery. This bill proposes to increase that limit to $500 only in cases where the consumer had written the personal identification number on the access card or if the consumer had stored the ID number with the access device.

Keep in mind that unauthorized use of an access card is totally different from unauthorized use of a credit card. A credit card may be stolen and used by anyone; therefore the $50 limit of liability makes good sense as long as the credit card issuer is promptly notified by the consumer that the card has been stolen. However, if an access device is stolen, it is a worthless piece of plastic unless the thief also has the ID number or code word.

Why should banks foot the bill for this kind of irresponsibility or negligence? It results in losses and subsequently higher fees for everyone, not just those who were negligent.

Section 432 of the bill addresses Home Ownership Debt Counseling Notification. Existing law requires lenders to notify delinquent borrowers within 45 days after the initial loan default that homeowner credit counseling programs are available. The proposed amendment would clarify a current ambiguity by confirming that failure to timely give the notice would not adversely affect foreclosure proceedings under State law. This clarification is highly desirable for several reasons.

Lenders rarely consider a late payment to be a serious default until it is over 30 days past due. This leaves little time for the lender to contact the borrower, determine the cause for the non-

payment, and obtain payment within the timeframe allowed. In most cases the missed payment was an oversight, was lost in the mail, was a result of the payment check being returned for insufficient funds (often to the surprise and embarrassment of the borrower), or was due to some other reason not evidencing an inability or unwillingness to repay.

Regardless, in order to meet the 45-day deadline, the lender is required to send a notice to each delinquent borrower which, in effect, reminds the customer of the loan default and urges him or her to consider home ownership credit counseling. (What an embarrassment!) This letter is accurately perceived by the customer as the first step in the lender's collection process. To require the lender to prematurely initiate its collection process at this early stage is inefficient, upsetting to the borrower, and damaging to the goodwill the lender works so hard to develop with its customers. This certainly is not the intention of the law.

Currently, the Real Estate Settlement Procedures Act [RESPA] requires banks to provide a disclosure of the percentage of loans for which servicing has been transferred. This disclosure must reflect the actual percentage of transferred loans for each of the last 3 years. Therefore, each year the form must be destroyed, reprinted with the latest year's percentage, and distributed out to our 93 offices statewide.

Why not simply require us to disclose to borrowers the fact that the servicing of their loan may be transferred and that they will be promptly notified by us at the time of the transfer before the payment is due to the new servicer? This would serve the same purpose but would be far more efficient.

Title 5: This title deals with the Community Reinvestment Act [CRA]. The first change to be imposed by this bill would be to reduce the paperwork compliance burdens of CRA. Currently, the CRA requires the ascertainment of community credit needs. To receive a satisfactory or better rating, this process must be "continuous" and "ongoing." It has been our experience that community credit needs are mostly static and the time and expense invested to demonstrate our good-faith effort at compliance yields little or no new information. It should be acceptable for a bank to have a comprehensive process in place for periodically assessing community credit needs in its delineated communities, such as once every 1 to 2 years, thus saving time and expense which could be devoted toward more results-oriented activities.

Another paperwork burden of the CRA relates to the constant documentation of our efforts to increase loan penetration in our delineated communities, particularly in low- and moderate-income areas. If the numbers of applications received by a bank from low- and moderate-income persons is not great enough, the bank will surely be criticized and may even be given a less than satisfactory rating, thus freezing all growth until the next exam.

In an innovative strategy intended to increase lending to low- and moderate-income minority neighborhoods, First Interstate Bank of Texas piloted a preapproved loan offer during 1992 which was repeated in 1993. As you know, preapproved loan or credit offers are frequently used by banks to reach more affluent prospects, especially in the area of credit cards. We believe that First

Interstate may be the first to use this strategy to reach persons below the median income level.

Our strategy called for selecting low- and moderate-income census tracts which were predominantly minority, then using a demograpics consultant to determine which tract residents were homeowners. Next, that comprehensive listing was processed by the credit bureau using a moderately strict screening criteria. Of the 4,745 minority neighborhood homeowners screened in our first effort, 1,142 were eligible to receive a preapproved offer of a $1,500 unsecured home improvement loan. Only seven accepted our offer. We began calling those who did not respond to our offer to better understand their reasons. Of course, many indicated that they simply did not have a current need, but an equal number indicated that they were averse to credit. In other words, they chose to preserve their good credit profile by not accepting credit unless absolutely necessary.

To determine if our first experience was an aberration, we repeated this effort in 1993. Selecting different census tracts using the same profile, we screened 32,125 minority neighborhood homeowners. Of that number, 3,662 were eligible to receive our preapproved loan offer, but only 11 accepted.

A related finding from this process is that in our most recent effort, over 85 percent of homeowners in these tracts failed the credit screening under the first tier or the most lenient criteria, meaning that the credit record contained numerous derogatory listings.

We believe this experience suggests that it is not a financial institution's unwillingness to extend credit to minorities and lower income applicants that stands as a barrier to achieving parity in lending rates, but broad-based societal issues which have left these individuals more vulnerable to health and employment crises which may lead to related credit problems. Also a factor is the hesitation to accept credit among those with sound credit ratings.

In light of the above efforts to increase our loan penetration in low- and moderate-income census tracts, I asked the OCC if we could count these credit offers on our home mortgage disclosure report and categorize them as withdrawn applications. Their answer was no.

Therefore, our HMDA report continues to reflect rather small numbers of applications from low- and moderate-income census tracts, even though we advertise in those areas, conduct workshops, actively participate in the communities, and offer preapproved loans.

I thank the chairman and members of the subcommittee for the opportunity to speak today and I would be happy to answer any questions.

[The prepared statement of Ms. Lopez can be found in the appendix.]

Chairman NEAL. We thank all of you for your very fine testimony. You have given us detail that we haven't had before. I have this general impression that much of what we are doing is unnecessary and counterproductive. I think these specific examples will help us as we try to develop the legislation. Of course, Mr. Bacchus has already done a lot of this for us.

I really don't have any questions at this point. I think you have helped us a good deal.

I will yield to Mr. Flake.

Mr. FLAKE. Thank you very much. Good morning, Mr. Chairman. Just a couple of questions, or perhaps even one that all of them can respond to.

In H.R. 962, and my H.R. 2707, Bank Enterprise Amendments of 1993, we try to address the question of community reinvestment. Some of your testimony suggests that one of the problem areas has to do with not having standards that regulators can actually assess what their requirements happen to be, and therefore the individual regulator can in fact do an assessment at one bank and another regulator do something quite differently at another bank.

We tried to address that by giving a safe harbor provision which addresses what I think Ms. Lopez and Mr. Kase raised. By giving a 3-year safe harbor to those banks that are outstanding, they would not be in the position of having to contend at the point of the third year, but rather have a basic business plan set up front, knowing what they would have to do to meet CRA requirements so that, Ms. Lopez, in a case like yours, where you actually went through some processes over a 2-year period and then they were disallowed, you would know in advance they would not be allowed. Therefore, you would not have to spend that amount of time or paperwork trying to get something together that ultimately was not. What is your general opinion of our safe harbor concept if they continued to maintain that outstanding rating over another 2-year period?

Ms. LOPEZ. I would like to answer first, because for my bank, being a large bank, it is very, very difficult for a large bank to obtain an outstanding rating. We are very pleased with our satisfactory rating and we have spent hundreds of thousands of dollars obtaining our satisfactory rating.

Therefore, I would like to see the safe harbor applied to both satisfactory and outstanding ratings, perhaps maybe on different levels. For instance, a bank with a satisfactory rating could enjoy a safe harbor until the time of its next exam, which would be——

Mr. FLAKE. My problem with that, quite frankly, is that 90 percent of the banks are in satisfactory. I am a practitioner outside of this, a community developer, and the problem is that we are not getting enough capital into those communities. Ninety-eight percent of the banks are sitting on their satisfactory rating and not really working to get into the outstanding category.

What I am trying to do is incentivize banks to get to outstanding and then give them the carrot of knowing that if they get there, they will be precluded from having to deal with objections at the point of that third year of outstanding ratings.

My intent is to get as much capital into the communities as possible.

Ms. LOPEZ. That is our intent as well, as you can see from our preapproved credit offers.

Mr. FLAKE. Well, those offers are not significant as it relates to the objective of trying to get housing and commercial front development done, which is what I think places people in a category where you could probably get more credit card approvals because

you would have more homeowners and more people who would have jobs in those communities.

Ms. LOPEZ. Our preapproved offers were not a credit card, they were home improvement loans.

Mr. FLAKE. $1,500, right.

Ms. LOPEZ. Right.

Ms. BARR. I think that any incentive that could be built into the system to receive an outstanding would be worthwhile because an outstanding is a moving target. We have had two exams in a row where we did receive an outstanding, but the way that—the rationale for that outstanding was different each time, and the anxiety within the bank, when the examiners come in, although we believe that our efforts are not only continuing but even increasing in many cases, as we have grown, we are still not sure we are going to rate an outstanding because the target is moving.

So if there was a carrot in there to receive that outstanding rating and there was some consistency, as you said, one examiner to another, and a satisfactory is a very wide band between an A-plus satisfactory and a B-minus satisfactory, a little consistency and an incentive would be much appreciated.

Mr. FLAKE. Mr. Kase.

Mr. KASE. I also strongly support a safe harbor along with as many fixed, identifiable standards as can be ascertained. I certainly would be the first to point out that the distinctions between large banks and small banks, between urban and community or rural banks, are substantial. So I don't have an answer for you as to how you would set those standards. I think they might have to be adjusted to face some of the problems that Ms. Lopez's bank faces that my bank does not face.

But beyond that, I think what is critical to the safe harbor is to reinforce the comment that it is a moving target. Each time our rating has been based on different activities. And in fact the second time around, the impression was, what have you done lately. So that all of the programs and all of the efforts which rewarded us with an outstanding the first time were considered, well, that won't get you an outstanding the second time. And my question is, why not? The answer is, because you have to keep showing that you are doing new things.

I like the idea of continued innovation and initiative, but I am not comfortable with the concept that a well-established, well-run program will presumably decay, because you don't make further progress. So I think the safe harbor would help in that certainty factor.

Mr. FLAKE. Regulators have been in to testify before us, they have been in my district, they have been in New York, and they have testified before my subcommittee. All of them have received testimony that banks do not lose money in CRA loans. Basically, is that your sense, in terms of your institutions?

Mr. KASE. Absolutely.

Mr. FLAKE. So it is not a burden once you make the loan? You get the same return you get in any other community?

Mr. KASE. The burden is in the regulation and the proof and the records and the files and the cabinets and the meetings that we have to go through to prove that we are making good community

loans. We strongly support the local development projects, the economic development activities, the downtown redevelopment zone. And we have rewarded the community and the community has rewarded us every time. So CRA is great. It is just the manufactured paperwork that causes the trouble.

Mr. FLAKE. All right. Make sure when you consider your downtown redevelopment zones you have the people who are not downtown included to make it work. That is where my problem is. Too often we have redeveloped downtowns and have not done anything with the surrounding communities.

Thank you, Mr. Chairman.

Mr. Neal and I will be working to do the best we can to get you to outstanding categories, because I believe if you can get the money into the inner cities particularly, you will have a fertile field of opportunity that has too long been ignored.

Thank you very much.

Chairman NEAL. Thank you.

Mr. Bacchus.

Mr. BACCHUS. Thank you, Mr. Chairman. Thank you for allowing Mr. Bereuter and me to twist your right arm and get you to hold these hearings.

Mr. FLAKE. Is that what happened?

Mr. BACCHUS. A legislative ploy.

I understand Mr. Orton announced before my arrival that he is enlisting as a cosponsor of H.R. 962. I believe that makes 267 cosponsors on both sides of the aisle. I applaud him. I thank him. I look forward to working with him and with you, Mr. Chairman, and with everyone on the subcommittee.

For the witnesses, let me say thank you. You've elaborated some very specific reasons why we need to pass H.R. 962 and provide for reasonable regulatory relief. I am prejudiced in this respect. It is my bill. Also Mr. Bereuter's bill. We appreciate your being here.

Ms. Lopez, we are also going to hear testimony from the General Accounting Office, which is not as inclined to agree with us as you are, on section 132. They are going to tell us that they believe it is a, quote, "crucial component of prompt corrective action," and that it, quote, "needs to be enforced at all institutions," and that they oppose our proposals to selectively implement these requirements by allowing those institutions with CAMEL 1 and CAMEL 2 ratings not to have to submit to this type of micromanagement.

Why are they wrong?

Ms. LOPEZ. Well, unlike the CRA rating, a bank's CAMEL rating is confidential. Therefore, I cannot share my bank's CAMEL rating with you. But I will say that for a bank to enjoy a 1 or 2 CAMEL rating by the OCC is an incredible accomplishment.

A bank of our size already has the policies and procedures in place that have been reviewed by the OCC and approved by the OCC. We already have the stringent internal and external audit programs in place as well as compliance monitoring tools in place.

It just seems like another duplication of what is already a tremendous effort that a bank is engaged in when a bank is rated a 1 or a 2.

Mr. BACCHUS. So you don't think any additional safeguards in the way of specific compliance standards and procedures are needed for institutions that have CAMEL 1 and 2 ratings?

Ms. LOPEZ. That is correct. I do not think additional safeguards are needed.

Mr. BACCHUS. The GAO will also testify these forthcoming regulations implementing section 132 will not amount to micromanagement at all. They are going to tell us that the current drafts that are being discussed, the proposed regulations, won't impose specific micromanagement, but instead will be far more general and won't lead to a lot of the additional documentation that a lot of institutions are so apprehensive about.

Do you believe them?

Ms. LOPEZ. I do not believe that. The penalties for noncompliance with regulations such as FDICIA are so onerous and high and can be applied both to the bank as well as its stockholders or its directors as individuals. Therefore, it is in our best interests to dot every "i" and cross every "t" in accordance with the law.

Mr. BACCHUS. Changing the subject just for a moment for a final question, I look to your comments on Title IV in the Truth in Lending Act. Representatives of several consumer protection groups testified before us a week ago. They said that to make any changes in the Truth in Lending Act such as we are contemplating would be very much detrimental to the interests of consumers. They see that law as sacrosanct and the height of perfection in its current form, including all the regulations and forms implemented thereunder.

I was struck by what you said about Truth in Lending. As I read your testimony, your institution, which serves many, many consumers, has found the amount of disclosure involved in the Truth in Lending Act so onerous that for a period of 5 years you didn't even offer certain products. What products were you unable to offer during those 5 years?

Ms. LOPEZ. I think the Truth in Lending Act is a very good and worthwhile act.

Mr. BACCHUS. So do I.

Ms. LOPEZ. The problem I have with the Truth in Lending Act is the specific disclosure related to adjustable rate mortgage loans, both initial disclosures at the time of application as well as subsequent disclosure at the time of an interest rate change. The Truth in Lending Act already requires a cap to be disclosed, a cap is a ceiling of interest that would be allowed on that loan, throughout the life of the loan.

Therefore, when the customer signs the document to become obligated to repay the bank, the customer sees what the maximum interest rate is going to be. And this is without these ARM disclosures. These are the ARM disclosures. The customer sees both what the——

Mr. BACCHUS. For the record, Mr. Chairman, she just lifted several very heavy files and showed them to us.

Ms. LOPEZ. I will leave these. The cap will tell the customer what his maximum interest rate will be during the life of the loan. It will also tell the customer what his payment amount will be, and his maximum payment amount if interest rates go up to that cap

for the life of the loan. Therefore, these additional disclosures I think serve to confuse the customer.

I think the customer needs to be told and it needs to be very clear to the customer that the interest rate can change and can go up.

Mr. BACCHUS. What products were you not able to provide?

Ms. LOPEZ. The adjustable rate mortgage.

Mr. BACCHUS. What you are telling me is because of the burdensome disclosure requirements imposed by the regulations implementing the Truth in Lending Act, for a period of 5 years, your institution found itself unable to offer adjustable rate mortgages to consumers in your service area?

Ms. LOPEZ. That is correct. The main problem with our ability to comply was with the subsequent disclosure requirements that have to occur at the time of an interest rate change. Our computer systems weren't smart enough to provide those subsequent disclosures; that is, at the time of the rate change the customer would have to be told what the new amortization schedule would be, when the final payment would ultimately be due, and, you know, with an interest rate change, your final payment date is going to change if it is an increase in the interest rate.

Mr. BACCHUS. Because of all that your institution decided it simply wasn't worth the time, trouble, money to offer those loans to consumers, and so the consumers in your area suffered?

Ms. LOPEZ. That is right. It wasn't worth the risk, because the errors that have been discovered in adjustable rate mortgages have been high.

Mr. BACCHUS. One final question before I yield to the chairman and to another of my colleagues who have been waiting patiently.

Our bill would provide that if one has a net worth of $1 million or an annual income of $200,000, then there would be no requirement for a regulation Z disclosure in the loan closing. This is analogous to the exemption that has existed for decades in the securities laws with securities offerings.

Do you see any reason why someone with that type of income and net worth should have to be provided with a regular Z form?

Ms. LOPEZ. Frankly, if that passed, I would go ahead and give the disclosure. Operationally, it is easier for me to comply with the regulation across the board and providing the truth in lending disclosure is no big deal. It wouldn't be a problem for me.

Mr. BACCHUS. Do any of these folks read the forms?

Ms. LOPEZ. I should hope so, but often I wonder when I look at a loan such as a swimming pool loan and the person can see that if they finance the swimming pool loan over 15 years it is right there in the Fed box in great big numbers, the cost, the actual cost of that swimming pool, although it might cost $30,000 to install it but after 15 years it could be over $100,000. I don't think I would be too tempted to install a swimming pool. But a lot of people do engage in swimming pool loans.

Mr. BACCHUS. That is the American way.

Ms. LOPEZ. Right.

Mr. BACCHUS. Thank you, Mr. Chairman.

Chairman NEAL. Thank you very much.

Mr. Klein.

Mr. KLEIN. Thank you very much, Mr. Chairman.

I commend you for holding this hearing. I commend Mr. Bacchus for his sponsoring the legislation, which I think is very, very important legislation, and the purpose of which I strongly endorse.

I do have some concerns, however, in two areas. It seems to me that the legislation really focuses on two things. The first is reducing unnecessary costs of operations, and that is not only a very worthwhile goal, but I think in the long run beneficial to both banks and to consumers.

The second purpose for which it has been touted is that it would then help with respect to the credit crunch. And to me, the credit crunch is probably the most crucial problem that we face in this Nation in the banking industry as it relates to the banking industry.

And I would like to ask a couple of questions about that, because I know that the administration has taken some very significant initiatives in terms of reducing regulatory burden for the purpose of accomplishing both of those goals, but notably for the purpose of expanding credit. One of the major things is to permit the more extensive use of character loans and to eliminate many of the regulatory problems relating to a certain portion of loans so that they could be used as so-called character loans.

I have heard from the Comptroller that the number of banks that utilize that regulation and other regulations that have been relaxed is disappointingly small. I would like to ask each of you what your own experience has been with regard to the use of character loans since the new regulations have been put into effect.

Ms. BARR. Well, I will address that. We reviewed the policy statement when it came out and considered whether or not we wanted to adopt any special monitoring for character loans and have chosen not to, which I believe many banks have.

Our reasons for doing so really are twofold. One, we believe we have been able to continue to make the loans that are necessary in our community and meet the examiners' criteria, although it has been more difficult, there is more paper involved and much more time on the part of the bank.

But now that we have implemented our 100-page loan policy and have indoctrinated all of our staff that this is our loan policy, that is the loan policy with which we are comfortable, and we are continuing to make the kind of loans, but instead of an unsecured loan, we might now be picking up collateral. We might have a shorter repayment period.

Making a major change to also then add a level of monitoring for our basket, reporting on the aggregate, which is a big concern to us, is that it adds another operational step, and frankly, not having been through an exam or heard from colleagues who have been through an exam, to know what that experience is like, we are a little bit reluctant to be out there as the guinea pig.

Mr. KLEIN. I will tell you, that is a little disheartening to those of us who see the regulatory relief as an avenue for expansion of credit. And while I haven't heard your explanation before, I have heard other explanations, and they all boil down to the same thing, and that is that the cry for character loans really has not produced the response that we think that it should have. But go ahead.

Ms. BARR. I was just going to mention my bank does continue to have a 75 percent loan-to-deposit ratio. So we don't believe we have been withholding credit. We believe we made the changes 3 years ago to our lending philosophy to match the expectations of our regulators, and that is now our lending philosophy. And we believe that that is the lending philosophy that the regulators are going to expect on an ongoing basis, and we are simply going to manage the bank in that direction.

Mr. KLEIN. Anyone else wish to comment on that?

Mr. KASE. I would only reinforce what she has said concerning the complication of lending activity interfering with our loan production. I don't think I would agree. Lending is a process which goes on under whatever guidelines you give us, and we will do our jobs and we will lend. I think we feel we have successfully lent to the community and the addition of that particular avenue wouldn't probably change the results for us. Certainly, it is an opportunity to simplify perhaps some of the recordkeeping or avoid some of the standards. But it would not have a substantial impact.

Mr. KLEIN. Ms. Lopez?

Ms. LOPEZ. Our bank, again, is so large. We have specialists for all the different areas of lending, whether it is international lending, energy lending, small business lending, affordable housing lending, and so forth. So what I would encourage to you do is contact me and I will put you in touch if you are concerned about small business lending, for instance, character loans in that area, I will put you in touch with our senior vice president in charge of small business lending.

Mr. KLEIN. What I am really concerned about is what we can do in the way of regulatory relief that will encourage banks to expand their lending, not only in the character loan area but in other areas as well.

I would certainly welcome from the banking industry any recommendations that the banking industry would like to provide as to how we can expand credit and get the banking industry more into the area of providing credit, both to the business and to the consumer communities.

Ms. LOPEZ. I have overheard during the course of meetings at my bank that there needs to be a reconciliation between the FDICIA requirements and the CRA regulations. The FDICIA and FIRREA safety and soundness type issues related to loans, some of which may be character loans, need to be reconciled with the mandate from our regulatory agencies to make more small business loans and more low- and moderate-income loans.

Mr. KLEIN. I extend to each of you and to all others in the banking industry any suggestions or recommendations you may have in that area.

Thank you very much, Mr. Chairman.

Chairman NEAL. Thank you.

Mr. Barrett.

Mr. BARRETT. Thank you, Mr. Chairman.

Mr. Kase, I welcome you. I have a special place in my heart for Sturgeon Bay because my mother was born there. My grandfather used to work at the Bank of Sturgeon Bay. Nice to see you here. I

also want to applaud you because I think you gave the best testimony that I have heard thus far on the need for regulatory reform.

One of the frustrations that I have experienced, even talking to my bankers in my area, is that I can give the speech now for regulatory reform, but I haven't seen the specifics as to what are the straws that are breaking the camel's back. I think you have done a good job in laying that out. It is a good document for me to work from.

Ms. Lopez, I listened to your testimony and I think your bank is doing a good job in trying to get into the community. One of the things you said in your testimony was the problem with the societal biases, and I hope that your institution recognizes the role that it must play in employment as well.

One of the frustrations I have seen with a lot of people when they talk about—and this is more aimed toward the insurance industry—is they say, we can't solve society's problems. Then I look to see how many minorities they hire, how many agents they have in the central city, how many offices they have in the central city, and they are no part of the central city at all.

So I don't think one can go in and expect there is going to be great demand for products if the people in those neighborhoods don't have the ability to make a livelihood.

Ms. Lopez. We recently opened or contracted to purchase a property to open a new branch in an area of Houston that is populated by 75,000 low- and moderate-income persons. There is not a single financial institution in the area. The only semblance of a financial institution in that area are pawnshops and check-cashing services. So we are very proud of that accomplishment.

Mr. Barrett. The last point I want to make, it applies to all three of you, maybe the banks and lending institutions in my area have satisfactory or outstanding ratings from CRA as well, and I think that is wonderful. Then I drive home through the central city of Milwaukee and see a place that has a lot of poverty and I am thinking, if everybody is doing such a great job, why is this community so poor?

So I think that the situation is, you have two ships passing in the night. You have great forms that are filled out, and I recognize the frustration that banks have with generating paperwork, but I think that the problem we have done now is we have set out, if you pass this test, you are done, and the problem is solved. Anybody who has ever been to any of the neighborhoods in urban areas knows the problem isn't solved.

So I think what we have to do is regroup, because I am not someone who loves creating paperwork. I am someone who loves creating economic opportunities within my community and it is not happening right now.

Ms. Barr. I think you have made the case for why we would much rather have a CRA system that measured you on your results. Right now we are in the process of trying to gather whatever information we can about how many jobs have been created in the inner city of Minneapolis where many of our small business loans are as a result of the loans we have made, because I think that is the heart of what Riverside Bank does.

I believe if we could say that we have—we are a small business bank, we have made this many small business loans, and this many jobs have been created in the inner city because of them, that that is an outstanding rating. It is not because of the pieces of paper.

Mr. BARRETT. Thank you.

Chairman NEAL. Thank you.

Ms. Maloney.

Mrs. MALONEY. Thank you, Mr. Chairman.

As we are looking at regulatory relief in order to become more competitive and produce more business, some reports are showing that banks are making record profits. And I would like your comments on that. If the regulatory relief is so burdensome and hard, why are banks showing record profits? Which I am delighted to see.

Second, could you comment on the amount of your capital in your bank that goes to government securities. Due to our large debt, the amount of government securities that we have to sell grows radically every year, and some of the banks in New York and other places have told me that they are putting a great number of their resources into government securities, which I am delighted, I am glad someone is buying them; we would have a big problem if they didn't. But I would like to know how much of your loan capital—is it half, 10, 70 percent—is going into government securities.

Mr. KASE. I would like to start off first with the record profits and the regulatory burden in my mind are two totally separate issues. The hard work that has gone on in our bank, the training, the experience that we have developed, has led to success. I think the economy has led to success recently, although the cycle of apparent boom and actual boom may not be simultaneous. But the regulatory burden is a separate cost which is going to be there, which is unnecessary to a great extent, and I think the two should be separate.

Mrs. MALONEY. How much is the cost generally for regulatory burden in your bank, an estimate?

Mr. KASE. I had provided an exhibit which indicated for six major regulations and my management program, we spend in excess of $220,000, I believe the figure is. I go through 6 regulations because they are commonly understood and recognized, but there are 15 to 20 more regulations, all not as burdensome, but the number and list is endless.

Beyond that, you have the safety and soundness activities, and that is regulatory burden of a different nature: Do we audit? Are we protected? I can't give you a hard figure about—in the consumer lending area, we might spend probably close to a half million dollars by the time we are done.

Chairman NEAL. What size bank is yours again?

Mr. KASE. We are $220 million at this time. It fluctuates, but we are about $220 million.

Mrs. MALONEY. And the amount you are putting into government securities in your loan pool?

Mr. KASE. Being a community bank we primarily put our resources back into the community to the greatest extent possible, so

our government involvement in our investment diversification is probably less than 10 percent.

Ms. LOPEZ. I can't speak to our bank-owned securities portfolio, but may I call you with that information?

Mrs. MALONEY. Thank you.

[The information referred to can be found in the appendix.]

Ms. BARR. I know we have an $80 million loan portfolio and our government securities are under $8 million.

Mrs. MALONEY. Thank you.

Thank you, Mr. Chairman.

Chairman NEAL. Thank you.

If any of you would feel comfortable answering this, what part of the regulatory burden you face is generated by Federal law and what by State law?

Mr. KASE. With respect to our preparation for examinations, I would say that we probably need, from the regulatory side, three to four times as much preparation. With respect to the laws that I deal with on a day-to-day basis, I would say again it is probably three or four to one, Federal regulation versus State.

Ms. LOPEZ. I would say 98 percent is Federal regulation, 2 percent State regulation.

Ms. BARR. And I would say in Minnesota, which is often on the cutting edge of consumer protection regulation, probably 90 percent Federal, and 10 percent State.

Chairman NEAL. Over and over again we have seen the examples of the huge files necessary, the mass of paperwork necessary just to close a simple mortgage loan. Of all that paperwork, how much of that is federally required, how much is required by a secondary market, for example, or generated by your own internal needs?

Ms. BARR. We are not involved in the secondary market, so I do not know.

Ms. LOPEZ. Many of the underwriting requirements are required by the secondary market. That is, we won't be able to sell a loan to the market unless there is a certain debt-to-income ratio or a certain collateral value requirement. But those are related to the underwriting, the credit decisioning of those loans.

The majority of documents involved in closing a loan or accepting a loan application are required by the Federal disclosure regulations rather than the secondary market.

Mr. KASE. I would say of the 12 to 15 documents for a home mortgage loan, 10 of those are related to Federal regulation, and only the remaining note mortgage underlying application or other qualification for secondary market would take up the remaining 5.

Chairman NEAL. Thank you.

Ms. Pryce

Ms. PRYCE. Thank you, Mr. Chairman. I have no questions.

Chairman NEAL. Thank you very much.

I would like to thank the panel again. You have been most useful. If you have any more ideas in the future, we always welcome them. Drop us a note. Thank you again for being with us.

Our next panel is comprised of Mr. James Hansen, director of banking and finance, State of Nebraska; vice chairman, Conference of State Bank Supervisors.

Mr. Hansen, we would like to welcome you at this time. Thank you for joining us.

Mr. Hansen, we will put your entire statement in the record and ask that you summarize a little so we can have some time for questions and answers. You may want to introduce your associate.

STATEMENT OF JAMES HANSEN, DIRECTOR OF BANKING AND FINANCE, STATE OF NEBRASKA, VICE CHAIRMAN, CONFERENCE OF STATE BANK SUPERVISORS; ACCOMPANIED BY DOYLE BARTLETT, COUNSEL AND HEAD OF LEGAL SERVICES, CONFERENCE OF STATE BANK SUPERVISORS

Mr. HANSEN. On my left is Doyle Bartlett, counsel and head of legislative services for CSBS.

Chairman Neal, Mr. McCollum, members of the subcommittee, my name is James Hansen. I am the director of banking and finance for the State of Nebraska and vice chairman of the Conference of State Bank Supervisors [CSBS]. I appreciate the opportunity to testify on behalf of CSBS today on the subject of regulatory burden relief and specifically H.R. 962.

Through your leadership, Mr. Chairman, and that of the original sponsors of H.R. 962, fellow Nebraskan Congressman Bereuter, and Congressman Bacchus, you have begun the difficult task of addressing the excessive regulatory burdens imposed on the banking industry. Previous testimony has given detailed descriptions of the various provisions of the bill. Rather than review the specifics of that legislation, I will address CSBS's general view on regulatory burden.

Basically, State regulation of banking is guided by three important interrelated concepts. First, the institutions must operate in a safe and sound manner. Second, credit and payment services must be available to sustain communities and fuel economic growth. And third, consumers must be treated fairly.

The goal of State regulation is to strike a balance between these three nonconflicting principles. While innovations in the industry enhance all three, overemphasizing any single concept works to the detriment of the other two.

A review of the Federal banking legislation for the past 5 years shows that the unquestionable focus has been safety and soundness, and consumer protection. The question before this subcommittee and of concern to all of us involved in bank regulation is whether certain regulations and requirements can be reduced or removed to increase the flow of credit while maintaining the safety of the banking industry and the protection of the consumer.

There is no simple answer to this question. We must forge ahead, however, because the current level of regulatory burden negatively impact the long-term soundness of the banking industry.

The entanglement of the regulatory requirements are at least partially to blame for the inability of banks to respond to the competitive environment of the financial industry today. As a result, the market share of commercial banks has declined from over 40 percent in the mid-1970's to approximately 23 percent today. Most of the lost market share has gone to less-regulated competitors, such as securities firms and mutual funds.

New regulations and compliance procedures often are a roadblock to new growth. Testimony already received by this subcommittee describes in detail the repercussions of current regulatory requirements on all banks. The effects are particularly harsh on our smaller banks. These institutions are the ones which are the very lifeblood of small town America.

Across the United States, almost 2,000 banks have fewer than 10 employees. An additional 3,100 banks have between 10 and 25 employees. These two categories of banks make up 49 percent of the banking industry in our country. In Nebraska, the average asset size of the 257 State-chartered banks that we regulate is less than $50 million.

As regulatory requirements increase, the vast majority of these institutions are simply not able to add the additional personnel necessary to keep track of compliance. That means that either the chief executive officer must allocate more time to that area, or other personnel must be reassigned.

Of great concern to us also is the real possibility that this glut of regulations may adversely affect a bank's safety and soundness. As we all know, profitability is one way to measure the health of an institution. The burden of regulation is reducing profitability.

Additionally, overregulation may serve to reduce the quality of loans made by the bank. We must remember that banks are a business, and they need to be allowed to operate as such. Banking in general and commercial lending in particular are not paint-by-numbers undertakings. Just because all the paperwork is correct, placed in the file in the proper order, the loan is not necessarily any good.

One other critical factor comes into play: Judgment. Banks are not alone in shifting their emphasis to compliance. Several of the Federal regulators have also announced substantial increases in compliance staffs, including the reallocation of examiners from safety and soundness to compliance review.

These recent events, coupled with the sometimes severe penalties associated with the failure to comply, makes bankers' apparent obsession with compliance certainly understandable. The question for bank regulators and for members of this subcommittee is whether this is appropriate.

There are two other topics I would like to address briefly before closing. The first is the issue of the FDIC's backup authority over national banks and Federal savings associations. This authority is critical to the continued solvency of the deposit insurance funds.

The FDIC, as deposit insurer, should have the ability to independently examine any institution it insures. Some have suggested in testimony before this subcommittee that the FDIC backup authority be reduced. Earlier this week the FDIC Board voted to restrict its examination of federally chartered institutions.

We believe that these restrictions are counter to the congressional intent and counter to the best interest of the taxpayer guarantee of the deposit insurance funds. We strongly urge you to oppose any reduction in backup authority of the FDIC.

The second issue is the importance of flexibility in the supervision of the banking industry. Whether it is regulatory innovations or new products and services, both the regulators and the banks

must be allowed the flexibility and the creativity to meet the changing market conditions.

FDICIA placed a straightjacket on both Federal and State regulators by removing much of the discretion and judgment needed to supervise a dynamic and changing banking industry. We ask you to consider these issues as you address this and other legislation.

In closing, let me thank the members of this subcommittee who have already struck a significant blow against costly regulatory burden. Earlier this year you defeated the State examination fee proposal contained in the budget resolution. Your action saved the banking industry over $1.3 billion in additional, unnecessary costs, keeping these funds available for lending to support economic growth. In Nebraska alone, where the cost of regulation to State banks would have tripled, it saved over $12 million.

We appreciate your efforts to defeat the State examination fees and ask for your continued opposition to its imposition.

I will be happy to answer any questions.

Thank you.

[The prepared statement of Mr. Hansen can be found in the appendix.]

Chairman NEAL. Thank you.

Do you have some specific recommendations for change?

Mr. HANSEN. Mr. Chairman, we think some of the regulations could be eliminated or at least modified because they do not affect safety and soundness. Some of the proposals on the surface are good ideas. From the time you put the paperwork that is going to be generated in order to comply with these provisions, it becomes monumental. The blizzard of paperwork to hit our bankers' desks today is monumental.

To give you some examples——

Chairman NEAL. Excuse me. I am not putting this quite right. I am aware of that. That is why we are going at it.

I am wondering, you are right at the frontlines here, and I am just wondering if there isn't some way we can get a little bit more either from you or from the association of State banking regulators. I am just wondering if in some way we could get your advice on some very specific changes. Maybe an approach would be to take the Bacchus-Bereuter bill, go through it, analyze it, and then based on that come back to us with your opinion of each provision in that bill.

I am just thinking out loud with you here for a minute. And I am wondering if it might not be a good idea for that to be an official project of your association, so that we would get the wisdom of your counterparts from all States. Does something like this sound possible?

Mr. HANSEN. Certainly. We would be happy to respond to your subcommittee with specific suggestions.

Chairman NEAL. What do you think of that approach? Mr. Bereuter and Mr. Bacchus have generated a lot of very specific ideas here. What do you think of taking that as a starting point?

Mr. HANSEN. I think that is an excellent idea. In fact, the Governors Association has also asked the State bank regulators to look at this.

Chairman NEAL. Oh, have they?

Mr. HANSEN. Yes. We would appreciate the opportunity to give specific suggestions.

Chairman NEAL. We would very much welcome your advice on this. Some of the changes in that bill sound good, and I would be inclined to support them, but there may be some little subtlety there that would indicate that it might be counterproductive, or there may be some little twist on it that would make it better.

So anyway, we would very much welcome that and the sooner the better. We are going to try to move ahead with this soon.

Mr. HANSEN. We will be happy to respond and we will get to you in a timely manner.

Chairman NEAL. That is just great. I don't know if others have questions.

Ms. Pryce.

Ms. PRYCE. Thank you, Mr. Chairman.

Mr. Hansen, thank you very much for your participation in this hearing today. I would echo the chairman's thoughts about how important any input of you and your organization and organizations like yours are to us, because it is that experience that is invaluable to us as lawmakers and is so often perhaps overlooked as we make these very important decisions that are going to affect you. So thank you for your willingness to help us in that respect.

I would like to ask in particular, with the predominance in Nebraska of State-chartered banks that are falling below the $50 million in assets level, could you give us some sense of the ramifications and the cost that such small banks face for examinations if there is not an effort to do more to coordinate and streamline procedures? Do you have any sense of that? Is this dire? Can you elaborate at all?

Mr. HANSEN. I make it a concerted effort to get out and visit our State-chartered banks across our State, many of them very small, and it is on the tip of every banker's tongue, the amount of regulation they are having to deal with.

When you look at small town America and the community banks that are serving small town America, nothing happens in those communities unless that bank makes it happen. They are committed to their communities because that is really their livelihood.

So the compliance issues that they have to deal with, with the excess micromanagement type burden that is being issued as far as Federal regulations are concerned, is just making them take their time, time where the chief executive officer or lending officers could be out assisting their customers, trying to continue to serve their community, which is right now being spent in compliance with Federal regulation right now.

It is really not accomplishing what its intent is.

Ms. PRYCE. Thank you.

On a different line, would you care to comment on the effect the President's credit crunch alleviation plan might have on the day-to-day operations on banks as you have described them?

Mr. HANSEN. My experience has been that most banks are looking for good loans, and without the basket or with the basket, I think that you will find banks around this country are looking for good loans. They are looking for a way to lend into their community.

We have not seen a preponderance of so-called basket loans or the character loans being made by banks. I think those loans were already being made. At least the bankers I have talked to feel they already were doing that, and it really wasn't accomplishing as much as it was hoped to. I think that is probably the same around the country.

Ms. PRYCE. Thank you very much, Mr. Hansen.

Thank you, Mr. Chairman.

Chairman NEAL. Thank you.

You know, I really don't have any other questions now, but I very much look forward to your thoughts and those of your association on this question. It would be an enormous help to us. So I thank you very much for coming this morning and we look forward to hearing from you.

Mr. HANSEN. Thank you. We will look forward to responding to you.

Chairman NEAL. Do you need copies of the bill? Did we get those for you this morning?

Mr. BARTLETT. We are fully up to speed. We have just begun our review process in response to the Governors Association. So we will take on the bill as a model. We had not started in that direction, but we will use H.R. 962. We will do a section-by-section review and comment on each section.

Chairman NEAL. That would be great.

Mr. BARTLETT. I think we will take on some issues that were not in H.R. 962. One issue, we have real problems with is the prompt corrective action section that was included in FDICIA. We will comment on that at length as well.

Chairman NEAL. Even better. I think it will be helpful for you to use that bill. A lot of people are familiar with it. It has 267 cosponsors. We would welcome your thoughts.

Thank you very much. Don't hesitate to let us have your other views as time goes on. Thank you for being with us.

Our next witness is Mr. Donald Chapin, Assistant Comptroller General for Accounting and Information Management, U.S. General Accounting Office; accompanied by Robert Gramling, Director, Corporation Audits, Accounting and Information Management Division; and Mr. James Bothwell, Director, Financial Institutions Management Issues, General Government Division.

Gentlemen, thank you for being with us this morning. We look forward hearing from you.

STATEMENT OF DONALD CHAPIN, ASSISTANT COMPTROLLER GENERAL FOR ACCOUNTING AND INFORMATION MANAGEMENT, U.S. GENERAL ACCOUNTING OFFICE; ACCOMPANIED BY ROBERT GRAMLING, DIRECTOR, CORPORATION AUDITS, ACCOUNTING AND INFORMATION MANAGEMENT DIVISION; AND JAMES BOTHWELL, DIRECTOR, FINANCIAL INSTITUTIONS AND MARKETS ISSUES, GENERAL GOVERNMENT DIVISION

Mr. CHAPIN. It is a pleasure to be here, Mr. Chairman. I know the morning grows late.

Chairman NEAL. As always, we will put your entire statements in the record.

Mr. CHAPIN. I just would like to touch on a few points very quickly, and open this panel up to questions from the subcommittee.

You asked for our comments on the effect of H.R. 962, on credit availability and the safety and soundness in the industry. That is what we are here primarily to talk about today.

There are a number of different provisions in the bill that are intended to reduce the burden of regulation on safe and sound institutions. While we are not in a position to comment based on the work we have done on the particulars in many of those provisions, I want to emphasize to you and to the subcommittee GAO's support for efforts to reduce regulatory burden when that does not compromise the safety and soundness or other public interests.

We are concerned about several of the provisions of H.R. 962 that would, we think, weaken some of the safety and soundness reforms that were enacted by Congress 2 or 3 years ago, many of which are now being implemented. We think rolling back these reforms would place the taxpayers needlessly at risk and could undermine other legislative efforts in the future to modernize the banking industry, such as interstate banking.

We really do want to encourage efforts to identify and reduce the burden when there is a clear benefit in doing so. At the same time, we think that the Congress, the administration, and the regulators should exercise very great caution in considering short-term measures to encourage more liberal lending practices by insured institutions. The current improved conditions of the banks should not dispel the need to be vigilant, particularly in today's volatile business climate.

What we have seen recently is extraordinary interest rate spreads in 1992 continuing into 1993 that rescued, rescued a number of failing banks, and are largely responsible for the turnaround in the industry.

We have yet to see how the banks will weather rising interest rates in the future. That kind of scenario will test the banks' and the thrifts' ability to manage interest rate risk and sustain long-term earnings viability.

In that respect, what we see now as a risk to the banking industry is the complex derivative products that the banks are using to help manage interest rate risk but nevertheless involve substantial risk of loss. The competition for deposit dollars is strong. The choices of investment alternatives for the banking industry are there.

It is very important that the fundamental corporate governance requirements that are in place are kept in place. And it is important that they work well as a precondition for modernization of the financial system of the United States.

As the FDICIA reforms take hold, I think we can be more confident of the regulators' ability to successfully supervise the banks in today's competitive marketplace, and during times of future distress.

So, Mr. Chairman, we support efforts to reduce regulatory burden. There have been a number of steps taken by the regulators. We do support them. There are provisions in this bill that look to be positive. But we are concerned, seriously concerned

about provisions of the bill that would reduce the safety and soundness controls that were recently enacted by the Congress. We think those are important. We think they should stay.

[The prepared statement of Mr. Chapin can be found in the appendix.]

Chairman NEAL. Have you had a chance to go through the bill and make specific recommendations on each point, or is that something that might take a little longer?

Mr. CHAPIN. We have, as our full statement for the record points out, ongoing work that will relate to some of these provisions. Those reports are not yet finished. We are doing some very important work on derivatives, for example. Those reports will be issued in due course.

We don't have specific recommendations to make on the particulars of H.R. 962. We are here today to tell you of our concern about those provisions in the bill that tend to roll back safety and soundness provisions that were added in FDICIA to protect the insurance funds.

Chairman NEAL. What provisions do you have in mind in particular?

Mr. CHAPIN. We talk about the accounting, the auditing, the corporate governance provisions, the requirements for bank examinations, in effect the strengthening of the regulatory function.

Chairman NEAL. I will take a look at your longer testimony and try to become familiar with your thoughts there. It is not our intent—just speaking for myself here, others may have different thoughts—but it is not my intent to try to use your words, create a climate in which more liberal lending policies are in place. That is not what we are about here.

What I would like to see us do is to sort of clean house of the needless paperwork and regulations and so on that don't appear to be helping anyone. I mean, I am thinking of these massive files I have seen, particularly regarding mortgage loans and some other disclosures that I just don't think anyone is reading. We don't think they are accomplishing anything.

Mr. CHAPIN. We couldn't agree with you more, Mr. Chairman. We have been around, visited the banks, and looked at the situation. Clearly, there is a case for regulatory burden, and those burdens should be reduced.

I would like to suggest to you that if our testimony isn't particular enough as to the sections of H.R. 962 that we oppose, we would be quite willing to spell that out in absolute detail, if you wish.

Chairman NEAL. That was going to be my next question. If it would be appropriate for you all to do that, I have great respect for your work, and I think it would be very useful for us if you would just go through the bill, look at each section, and tell us what you think.

Mr. BACCHUS. Mr. Chairman, would you yield for a second on the same point?

I certainly would invite you to give us an enumeration of the provisions of the bill you oppose and reasons why. But I would also request, since you say there are some positive provisions in the bill, and since you say that there is clearly a need for regulatory relief, that you also enumerate the provisions in the bill that you would

think are good provisions, that you would support, and also tell us why.

Mr. CHAPIN. Mr. Bacchus, we can attempt to respond to that, but you need to understand that we are not—we have not studied all of the particulars of this bill.

Mr. BACCHUS. Yes, sir. I am asking to you do that.

Mr. CHAPIN. Well, that will take a bit of time, sir.

Mr. BACCHUS. Yes, sir.

Mr. BOTHWELL. If I can just add one comment, one of the studies that we are doing——

Mr. BACCHUS. Thank you, Mr. Chairman.

Chairman NEAL. Yes, sir.

Mr. BOTHWELL. We are looking at all the existing studies that have been done, the major ones by the regulators and by the industry groups, and what we have found there on the cost side is that we really don't think there are any really good, solid cost estimates of the amount of regulatory burden that is placed on lending institutions, nor is there a very good discussion of how these costs rack up against the benefits that regulation is creating in terms of more informed consumers, more lending in the inner cities, and that sort of thing.

But what these studies do for us is they really lay out what issues are of most concern to the industry. And those issues which we heard a lot about this morning concern mostly the CRA type of legislation, the social legislation, credit availability legislation, reporting requirements, paperwork types of burdens. And most of the comments that we have looked at on these studies, and most of the studies, do not really take great issue with the major safety and soundness reforms that were in FDICIA and that we have supported through our work.

What we are trying to do now is focus on those particular issues which are of concern to the industry and we are having a major study done on CRA. We are going out to 50 or 60 institutions. This is a study we are doing for the House Banking Committee. We are going into these institutions to find out what is going on with that process. Is it too paperwork intensive? Is there a way to improve the process to get more performance of the institutions in terms of their lending to low- and moderate-income areas?

This is something, as Mr. Chapin pointed out, that will take us some time to do. There is also another issue here. Some of these things you may have to changes laws, others you can just do by changing regulations, others you can do by changing how you implement those regulations. And that is what we really are trying to do.

We have already done one study, which we issued just a month ago, looking at what regulators can do to remove some of the impediments to small business lending. We have some recommendations in this report that they don't need to require appraisals for real estate that backs up a traditional small business loan.

So we think there are things the regulators can do to streamline their processes and their procedures. But it is going to take us some time to do that kind of work. But we are fully committed to do that. But it does take some time.

Mr. BACCHUS. Mr. Chairman, if I might add a few comments, I appreciate your time considerations. I also appreciate the good work you have already done on small business and a number of these issues. I am eager to have the benefits of your further work.

Mr. Bereuter and I are both very willing to work with you, as I know the chairman and the ranking Member, Mr. McCollum, who is a cosponsor of our bill, are as well.

Let me tell you that from our perspective, this is not just one more hearing on one more proposed piece of legislation. At last count we had 267 cosponsors of this bill. We are going to move some or all of this bill. Pieces of it just passed the Senate Banking Committee earlier this week.

If you think that in some instances we are going down the wrong road, we need you to tell us that in some detail and not just in the general terms of this testimony today. If there are provisions that are good, we need to identify them, because we don't expect to pass all the provisions of this bill.

So I am eager to work with you and I have high regard for your work, and I look forward to the benefits of it.

Thank you, Mr. Chairman.

Chairman NEAL. Thank you.

Again, I am going to say I want to thank the gentleman for his leadership on this issue. It is of enormous help to us to have this document to work from.

I understand the kind of major studies you are talking about take time. But I also hope that we can get the benefit of your work on these subjects.

What sort of time frame are you talking about for looking into the major provisions of this bill?

Mr. CHAPIN. Mr. Chairman, let me suggest one thing that we can do soon, and that is if we haven't been specific enough, we can tell you and the rest of the subcommittee exactly which provisions of the bill that we think are dangerous from a safety and soundness standpoint. We can enumerate those and document thoroughly, because we have studied this issue for a long time. We know what is wrong with this bill.

We are finding a lot of things right with this bill as we go forward with our work, but unfortunately that work is not yet finished. So I don't know how we can respond immediately to the positive aspects of this bill.

But we will do our work as promptly as we can, and I know you want to have findings from the GAO that are fact based, that are solid, that are based on the evidence. So we will provide that just as soon as we can.

Chairman NEAL. And when might you think that would be?

Mr. CHAPIN. I think our testimony sets forth some target dates for some of the reports that we propose to issue. By the end of the year our review of the regulation studies done by various industry groups and banking agencies will be available. We are looking at the methodology that they have used in addressing burden to see whether the burden issues that can be clearly identified as high priorities are in fact identified.

That report will be available at the end of the year and another study that will be available in the spring is an in-depth study on

the Community Reinvestment Act. As my colleague said, we have already issued a report on what the regulators can do and what they have done on both loans and on reducing the appraisal requirements for small business loans. So we have a report out on that issue.

There are other issues in H.R. 962 that we haven't looked at, that we probably should look at, including the provision for the reduction of liability for outside directors, a very important issue. We are very interested in that issue. It is germane to the behavior of boards of directors and particularly audit committees in how they exercise their function. That is directly related to our concerns about proper safety and soundness. We will try to look at that issue and put it on our agenda. But we don't have—we haven't done day one's worth of work on that issue as yet. We have a lot of background but we haven't worked on that particular provision.

So we will try to be as responsive as we can on all the of these provisions. As this bill goes forward, we will supply the Congress with as much information as we can on it.

Chairman NEAL. That is all we ask for and we appreciate it.

Mr. GRAMLING. Mr. Chairman, I would like to add that we list in Mr. Chapin's statement approximately 15 or 20 studies that the GAO has done that serve as background and support for our current positions, which are opposed to the section 112 and the section 132 changes that are in the bill. I think we are fairly clear there regarding the need for the accounting, auditing, and prompt corrective action requirements of FDICIA. With your permission, we would be pleased to provide those studies to the subcommittee as part of the record.

Chairman NEAL. That would be a big help to us. Please do.

[The information referred to can be found in the appendix.]

Chairman NEAL. Did you want to say something, Mr. Bothwell? Mr. McCollum.

Mr. MCCOLLUM. Unfortunately, I had a conflict with another hearing. We can only wear one hat at a time.

I am kind of curious in terms of the testimony, about explanatory language that says reducing regulatory burden, that it should be only when there is a clear benefit to do so. And that may go to paperwork reporting, it may go to—I don't know what it goes to.

And that is the point. Can anybody give me an example of what kind of benefits test you are contemplating? What do banks need to show in order to obtain regulatory relief? What is the clear benefit of that type of language? What do you have in mind by that criteria?

Mr. BOTHWELL. I would say that what we are looking for is not to rack up cost-benefit-type comparisons with regards to the specific regulations. In some of these cases it is very difficult to quantify the benefits of legislation like CRA. What we are trying to do in that area is to go to institutions around the country and look at that process and look and identify ways that that process can be made less burdensome and more efficient and more effective.

The administration also is undertaking a similar effort and hopes to come up with some recommendation by the end of this year. We hope our work will be done so it will be useful to this sub-

committee and the Congress in terms of considering what they come up with——

Mr. McCOLLUM. I understand what you are saying. I don't want to quibble over words, but I had read that testimony earlier, even though I wasn't here for its delivery, and I was struck by the fact that several times in Mr. Chapin's testimony, you say, in essence, that banks, in order to justify some of the changes (particularly those in Mr. Bacchus's and Mr. Bereuter's bill) must demonstrate or it should be demonstrated to us that there is a clear benefit to the bank.

I guess that is juxtaposed against what is perceived—it gets to some of the vagueness of this—the public policy benefit of some of the things that were passed in FDICIA. I don't know how you balance that off.

You just said cost-benefit analysis is what you really want to do. How am I or how is a banker who is complaining about one of these provisions to meet your test?

Mr. CHAPIN. Let me try to deal with that. We think that the FDICIA legislation is well thought out, that the safety and soundness rules and laws and regulations that were developed were good responses to a grave risk to the Bank Insurance Fund and at that time, we thought, to the taxpayers.

So when we look at steps to reduce regulatory burden and it involves the reduction of safety and soundless provisions, we have to look at it from the point of view of the protection of the taxpayer and the Bank Insurance Fund and try to see whether or not those amendments compromise the essential protections that the Congress built into the FDICIA legislation.

So we do start with sort of a burden of proof on those that would reduce the burden at the cost of protection. We would like to see why those are reasonable and why they won't expose the Bank Insurance Fund or the taxpayers to unnecessary or excessive risk. That is the point I wanted to make.

Mr. McCOLLUM. That is the clear benefit you are talking about. They have got to overcome that burden and show some kind of benefit that clearly outweighs what you perceive as the benefit of the language that is there in the law as a result of FDICIA?

Mr. CHAPIN. Yes, sir.

Mr. McCOLLUM. I just wanted to get some idea of that. There are those who would debate with you over the benefit of the law as opposed to the other way around. But what I wanted to do, and you have established for us, is to get your perspective. I am going to hear their perspective. I already have read it. I want to hear yours. And you have given that to me, and I appreciate it.

Mr. CHAPIN. Let me give you a few more words on that. When the savings and loan crisis was uppermost in everyone's mind, when the banking crisis came along right behind it, GAO devoted an unbelievable amount of resources to studying these conditions, why they occurred, what happened, who was at fault, what happened to the regulatory function, why didn't it work, why were we having these kinds of surprises in the financial reports of banks.

As our footnotes in this testimony show, we have developed lots of evidence that led us to believe that the Congress acted properly when they enacted the FDICIA legislation. So we think there is

reason for those provisions, good reason for those provisions. So when we look at suggestions to reduce those provisions, that we think protect the Bank Insurance Fund and the taxpayers, we have to look carefully at why those benefits don't on the other side represent risks or concerns to the fund and the taxpayers.

Mr. McCOLLUM. I think what we get down to is redebating, if we do get down to that, the merits of your conclusions on some of those, the need to protect safety and soundness, because what I am hearing from bankers, individual bankers, and quite a number of them, on these provisions, This went to the extreme, you didn't need to do that, the example of the S&L crisis was unique, it occurred because of the confluence of circumstances that are highly improbable to occur again, and you are putting by these regulations a constraint on lending and a constraint on our business, and the American taxpayer suffers the consequences for the years to come of overreacting to the extreme—that is what they are saying. They may not say it in those exact words, but you may have heard it too.

Mr. CHAPIN. We have heard it. I would just add one thing. I think those that would propose the relaxation of these, what we think to be, beneficial provisions of FDICIA, a burden of proof on their side to show that it wouldn't be excessive risk as a result of the reduction.

Mr. McCOLLUM. A burden I suspect you believe would be very unlikely they could overcome.

Mr. CHAPIN. We have our convictions, sir, on what we think is an excellent job the Congress did.

Mr. McCOLLUM. Thank you very much. I appreciate that.

Chairman NEAL. Were you suggesting that you think the idea of a cost-benefit analysis of regulations is not a sensible way to approach analyzing them?

Mr. CHAPIN. The concept is sound. It is just very hard to apply when you consider that now the banks are basically sitting pretty, whereas 2 years ago we were afraid that the taxpayers were going to have to come up with a huge amount of money. The shift in the ground has been dramatic, totally dramatic.

In the perspective of 2 years ago, it was easy to see why these reforms were absolutely, totally essential to protect the taxpayer. Now that the banks have lots of money, maybe more money than they admit to, but have lots of money, it is easy to say, why do we need these things?

But I think we should look at the banking institution, remembering that banks have 5, 6, 7 percent capital that can evaporate very quickly. Our studies have shown that a 1 or 2 rated bank can quickly become a 4, even a 5, and insolvent very, very quickly.

Capital protection is not large. The risks that banks undertake are very large. We have seen time and time again with third country loans, with highly leveraged transactions, with commercial real estate, the threats to the banking system.

The fact that we currently look at a very healthy banking system doesn't necessarily mean it is going to be that way tomorrow. And I don't want to be around here tomorrow without these protections when the banks once again have to come to the Bank Insurance Fund and possibly to the taxpayers.

Chairman NEAL. That improvement in condition is almost entirely due to a lower rate of inflation and a better interest rate spread.

Mr. CHAPIN. Yes, sir.

Chairman NEAL. That certainly could be something that—circumstances could change. It has been easier for banks to manage properly under these conditions. It could be tougher in the future, no question.

Just—I am glad to hear you are working on this derivative question. I must say I don't fully understand it. I have had it explained to me several times what is going on, and I still don't feel like I fully understand it. For that reason, if for no other, I am a little concerned about it.

There does appear to me to be considerable risk there. It looks to me like they are probably managing it pretty well, but I am uncomfortable with it. How soon do you think you will have completed your work on that subject?

Mr. BOTHWELL. Mr. Chairman, one of our primary goals in this work is to try to explain this whole business to people like yourself and myself in understandable terms. What we are trying to do is not only explain these types of products, but also tell you who is involved with this business, the extent of the risk that is out there, in these major derivative dealers, the extent that the dealers are trying to manage and control this risk with their own risk management systems and the investments that they are making in risk management systems, and indeed what the regulators are trying to do to improve their capability of overseeing this type of activity.

We are doing our very, very best to have our report out by the beginning of the new year, in that time frame.

Chairman NEAL. Could you give us—be prepared to give us some preliminary report a little earlier than that?

Mr. BOTHWELL. We could certainly try. One of our objectives is to try to have reports on crucial issues like this as soon as we can. But we are working full speed and we have a very big team working in this area.

Chairman NEAL. As soon as you think you have some meaningful data, you will know that—I don't have any way of knowing; it is just something you think is worth talking about—would you get in touch with us?

Mr. BOTHWELL. Yes, sir. We have just about finished our audit work and are drafting our report. But we need to take steps to share our preliminary thinking with others, and that takes us a while.

Chairman NEAL. You said that you have done a lot of work on trying to understand what had happened with the savings and loan industry. I spent a lot of time on that subject trying to understand it clearly. I came to think there were a number of things that could be said about it in terms of the origins of the problem. I sort of track it back to the high inflation of the late 1970's and the fact that the formula for savings and loans simply didn't work under those circumstances.

And then you have to look at the things that Congress and the administrations did to try to solve the problem, which in some instances turned out to only make it worse, go through that whole cycle. But I also came to think that if we had had adequate super-

vision, it simply couldn't have happened, it wouldn't have gotten away from us like it did. Is that a fair conclusion?

Mr. CHAPIN. I think that lack of proper supervision, lack of good accounting, good controls, on meaningful corporate governance, all the issues that were addressed in FDICIA, were at the heart of the savings and loan problem.

The fact that we have a Banking bill that dealt with banking issues doesn't mean that the provisions of that bill weren't also influenced by the experiences with the savings and loan industry. What we see is a continuity here of some of the basic issues that were problems with the S&Ls spilling over into the banks and leading ultimately to legislative efforts by the Congress to deal with those problems.

It would be wrong to think that we have put this all to bed, Mr. Chairman. Things like financial derivatives could produce new risks to the banking system. What GAO tries to do is to try to anticipate these problems before they become major threats to the taxpayer or the Bank Insurance Fund. That is the reason we undertook this derivative study.

I think it will be an important study, a big contribution to the understanding of the Congress of the risks involved not only to the banking system but also to the entire securities system of the United States.

Chairman NEAL. Well, I am just wondering, if we have a system here where we get what you do in a timely fashion, I know you do a lot of good work, I am not sure I see all the good work that you do, and I am certainly not sure that I see it as soon as I should. What could be done about that? Is there——

Mr. CHAPIN. We can improve the timeliness of our work.

Chairman NEAL. That isn't really my——

Mr. CHAPIN. But some of the things that we do involve exquisite judgments based on a lot of fact gathering. The derivative issue is one. There are lots of people who have written about the subject but they don't know enough about it to really come to firm conclusions.

We hope we have taken enough time to come out with a report that is soundly based, that people can rely on. So we are always tugging between wanting to deliver a product on time and wanting to be sure it is right.

So that is the problem we face continuously. We are trying now to accelerate the process by which we get reports out to the Congress. We have to say on complicated issues, difficult audits, it takes time to get the facts, and that is what you people want, I am sure.

Mr. GRAMLING. I think you may be referring somewhat to the distribution of our work, and certainly we are doing our best there, and on request, work to involve both sides of the aisle as we develop that work. In major work like my colleague, Mr. Bothwell, has under way in the derivatives area we have cosponsors for that type of work by subcommittee chairmen or others so that in fact that work can be made available to all as soon as it is finished. That is our goal, to get the information to the Congress.

Chairman NEAL. I am very interested in everything you do, so don't hesitate, don't be bashful about sharing your products with

us. If we can help in some way, we would be delighted to do that, too.

Let me ask you a couple of other questions. As you know, currently banks are required to file currency transaction reports for cash transactions in excess of $10,000. That $10,000 amount was put there several years ago. Pricing has changed the value of that. Is that something that should be changed or should we keep it at the $10,000 level? This is an attempt to get at money laundering.

Mr. BOTHWELL. Yes, indeed it is. I believe our people who do work in the law enforcement area have looked at those reports in terms of how valuable they are for the law enforcement effort, and there are some real questions there about their benefit.

In addition to that, the issue you raise about the $10,000 limit, $10,000 or above, I think any time you fix a certain dollar amount, and there is inflation, in real terms that threshold starts getting smaller and smaller. GAO doesn't have an official position on this. We really haven't looked at that particular issue. But I think it certainly sounds very plausible, to index it to the inflation rate.

Chairman NEAL. I have several other questions here but I also have some other things I have to do at noon. May I submit a few questions in writing?

Mr. CHAPIN. Of course.

Chairman NEAL. And before adjourning, let me recognize Mr. Bacchus. Again, I can thank you all.

[The information referred to can be found in the appendix.]

Mr. BACCHUS. Thank you, Mr. Chairman. I will be brief.

Gentlemen, thank you very much for your hard work, for your testimony, and for your commitment to the safety and soundness and protecting the taxpayers. Let me assure you that I share those commitments. In fact, I would suggest that those of us on this subcommittee in this Congress are probably even more committed to safety and soundness and to protecting the taxpayers than you may be, because if something goes wrong, we will be blamed. The Congress has certainly been blamed before. We are trying to do the right thing.

Mr. Bereuter and I have said repeatedly we don't want to do anything that will in any way, shape, or form, in any way diminish safety and soundness. We don't believe anything in our bill would do so. We may have some legitimate difference of opinion there, and that is why we need the further benefit of your counsel and advice.

I am especially concerned about the taxpayers myself. That is the primary reason I voted against FDICIA, because I thought we were bank rolling the replenishment of the fund through the back door of the Treasury, adding billions of dollars to the Federal deficit without appropriating the money. That still may well be the case. That has been done now. But I think that is a legitimate point of view, and I was motivated by my desire to protect the taxpayers.

You say that the banks are sitting pretty now. There is nothing wrong with that. We as Members of Congress would like our financial institutions and all our businesses to be profitable. And I know you would agree with that.

But my principal aim in supporting regulatory relief is not to make sure banks are sitting pretty. My aim is making sure that consumers have access to credit. And creditworthy borrowers have an opportunity to get loans so that we can create economic growth in America. I know that you share that goal.

And I invite your specific answers to some of the specific provisions that are raised in the bill. For the moment, let me simply ask you a couple of questions about your comments on our proposals for changing section 132 of FDICIA.

Now, we have had testimony earlier from a young woman, a very articulate young woman from Texas who sees no reason at all why CAMEL 1 and 2 rated institutions should have to bear the burden of the additional regulatory requirements that are about to be imposed by the implementation of rules under section 132. She says that all of the documentation, all the standards, all of the rules, all of the internal procedures are necessarily going to be in place in those institutions or else they wouldn't be CAMEL 1 and CAMEL 2 rated institutions.

She has testified as well because of the burdensome regulations under some other impositions, they have not made certain products such as the adjustable rate mortgages available to consumers. We are talking here about protecting consumers and making loans available and about that balance we have all been talking about.

Now, I am trying to understand why it is that CAMEL 1 and CAMEL 2 rated institutions should not be exempt from these forthcoming regulations. I am not quite certain I agree with you that these regulations are going to be as beneficent as you seem to anticipate. We will see later.

But based on what I hear you saying and on what seems to be in your testimony, my understanding is that you are telling us that even with CAMEL 1 and CAMEL 2 rated institutions, capital can many times evaporate quickly and these institutions can end up becoming 3, 4 and 5 rated institutions virtually overnight, and that this is sort of an early warning signal that would enable regulators to step in quickly in the event of seeing something that might go awry.

And my question is, if this is the case, if the internal standards that they have in place are not going to be sufficient to keep them from losing their capital quickly, then why are they rated so highly in the first place, and what should be done about that so that we could give some exemption from some of these additional regulations? Is the answer always to impose more regulations and more paperwork?

Mr. Chapin. Let me give a bit of a general answer, and then my colleagues will fill in, Mr. Bacchus.

Mr. Bacchus. And I won't keep you long because the chairman needs to go.

Chairman Neal. I am all right, thank you.

Mr. Chapin. Our studies suggest that CAMEL 1–2 banks are generally following the procedures, the controls and so on that are now in FDICIA. In other words, we don't acknowledge that there is a great burden, additional burden imposed on those institutions by virtue of FDICIA.

Mr. BACCHUS. But we don't know yet because we don't know whether these regulations are going to require additional compliance paperwork so they can demonstrate to you that they are doing in fact what you think they are doing.

Mr. BOTHWELL. If I may add, the section 132 regulations haven't been put out yet in final form.

Mr. BACCHUS. Yes, sir.

Mr. BOTHWELL. The regulators have submitted them to Treasury in a proposed format.

Mr. BACCHUS. Yes, sir, that is in your testimony.

Mr. BOTHWELL. When you look at what is being proposed, you really do not see that specific, detailed type of requirements that I think the industry feared may come from that section. We never thought that it should.

What we were looking for is some general principles of good, sound management with regards to internal controls, underwriting standards, and so on. And I think the regulators have proposed a set of very good principles that well-managed, well-run institutions, as we heard in the testimony this morning, should already have in place.

So we do not think that there will be any additional burden—there shouldn't be—on a well-run, well-managed institution. It is on the other institutions that really need to get their operations in order.

Mr. BACCHUS. Of course, Mr. Bereuter and I are not proposing that anything other than CAMEL 1 and CAMEL 2 institutions be exempt from these additional regulations.

Mr. BOTHWELL. But as you noted, things can change rather quickly. And in some of our work we have ongoing now, we are actually looking at every bank failure that occurred in 1991 and 1992 and looking at what were the factors causing those failures. And often you see institutions that are taken over, that change management, and people come in who aren't so dedicated to running a good, sound institution. And so those types of internal controls and the underwriting standards and everything else can go out the window.

That is why we think it is necessary to have these standards for all institutions, because things can change very quickly, such as a change in ownership of small institutions.

Mr. BACCHUS. What we have to do in calculating this balance is measure the benefits that we derive from having that extra early warning signal for those kinds of institutions, for those kinds of incidents of deterioration in management against the cost that is are imposed from the added regulation.

Based on your comments, I will be taking another and a closer look at the issue and looking forward to the final regulations.

Thank you, Mr. Chairman.

Mr. CHAPIN. Just one additional point, to try to put another face on this particular issue. The tentative rules that are now being looked at really give the banks that don't qualify for a 1 and 2 rating targets to shoot for, because that in effect defines a safe and sound banking institution, and it is well that those principles, that always were in the regulators' minds, be out in public view so that all banks can aspire to those kinds of ratings. I think what has

been done in the regulations is a very positive step and is not, as it stands now, paperwork intensive.

Mr. BACCHUS. Thank you, Mr. Chapin.

Thank you, Mr. Chairman, for your indulgence.

Chairman NEAL. Thank you, sir, very much.

Gentlemen, thank you for coming. We look forward to your work and other work. I will submit some questions. Thank you again.

[The information referred to can be found in the appendix.]

Chairman NEAL. The subcommittee stands adjourned.

[Whereupon, at 12:05 p.m., the hearing was adjourned.]

APPENDIX

September 23, 1993

STATEMENT OF THE HONORABLE STEPHEN L. NEAL AT HEARING ON H.R. 962

Thursday, September 23, 1993

I want to welcome everyone to today's hearing on regulatory reform and credit availability, and on H.R. 962, the bill dealing with this issue that has been introduced by Mr. Bereuter and Mr. Bacchus.

Last night President Clinton spoke on health care. One of the points he made was the need to simplify the system. He told how doctors at one hospital spend so much time filling out forms that they can see 200 fewer patients a year. He told how one hospital administrator spends $2 million a year on paperwork that has nothing to do with treating patients.

Our banking system is headed in the same direction. Bankers are spending more and more time filling out reports, studying new regulations and worrying about required paperwork than they are in tending to their business of making loans. Something has got to be done to get the spiraling burden of unnecessary paperwork under control in the banking, as well as in the health care, industry.

One fact stands out: the more time bankers must spend

figuring out regulations and filling out forms, the less they can spend making loans. And the more money they must spend to comply with federal laws, the less they have to lend.

As I indicated last week, the Administration has taken important steps forward on this issue with its regulatory proposals addressing credit availability, with efforts to ease loan documentation and appraisal requirements, among others. I also applaud the Administration's current effort to make the Community Reinvestment Act more workable.

Congress also needs to act on this issue, because it is our responsibility as lawmakers to review current banking laws and make any needed changes. Our goal in pursuing regulatory reform must be to increase credit availability as much as possible, while still maintaining strong safety and soundness protections.

Earlier this week the Senate Banking Committee acted on a community development bill, which also contained regulatory reform, and secondary market for small business loan provisions. These are important pieces of the credit availability puzzle and we should take

note of the Senate's approach of treating these items together.

The witnesses on today's first panel will tell us what is the view from the front lines. The panel consists of three bank compliance officers, who must deal every day with the real work of keeping their banks in compliance with the laws that Congress has enacted.

We will then hear from a State regulator, who will tell us how Federal and State agencies try to work together. Finally, we will receive testimony from the General Accounting Office, which has produced literally thousands of pages of reports on our bank regulatory system, and how it works.

I look forward to hearing the testimony of all the witnesses, and working with them and other interested parties, and with my colleagues on both sides of the aisle, to make progress on this important issue.

TESTIMONY OF KATE BARR

RIVERSIDE BANK
MINNEAPOLIS MINNESOTA

regarding

H. R. 962, THE ECONOMIC GROWTH AND FINANCIAL
INSTITUTIONS REGULATORY PAPERWORK REDUCTION ACT

before the

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
SUPERVISION, REGULATION AND DEPOSIT INSURANCE

of the

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

U.S. HOUSE OF REPRESENTATIVES

SEPTEMBER 23, 1993

INTRODUCTION

Mr. Chairman, my name is Kate Barr. I am Senior Vice President of Riverside Bank in Minneapolis, Minnesota. I appreciate the invitation to appear today and offer the experience of a small commercial bank in managing the growing volume of bank regulation.

Riverside Bank is a $125 million bank located in the city of Minneapolis. We have three branch offices in addition to our main office. Since we are a small bank in the midst of many, much larger competitors, we have sought a niche in the small business banking market. We have been successful in this effort, with 65% of our $80 million loan portfolio in commercial loans to small businesses. Our loans range in size from $10,000 to $1 million and in industry from retail and wholesale sales to manufacturing and service.

My responsibilities at Riverside Bank include managing compliance with regulations as well as responsibility for marketing, planning and some lending functions.

GENERAL COMMENTS ON IMPACT OF REGULATIONS

My responsibilities have included regulatory compliance since 1982, but the scope of that responsibility has increased exponentially in the past three years, particularly with the implementation of provisions of FIRREA and FDICIA. In addition to my efforts, many of the bank's other staff have had additional duties assigned to them in order to maintain compliance with the explosive growth of rules and regulations. No one single regulation, of course, is responsible for this burden. Rather, it is the cumulative affect of layers and overlapping layers of regulations issued by different agencies over the course of a relatively short time period.

The overall impact on Riverside Bank of the increasing regulatory requirements has been increased costs for staff time, materials, training and systems. We must have additional personnel to check over the compliance of the ones doing the work. The need to add staff and other costs might not seem so onerous to the bank if each new provision was clearly beneficial to either the bank or its customers. Unfortunately, this is not always the case.

There has also been an impact on our customers, particularly borrowers. Borrowing money is more difficult and costly in 1993 than it was a few years ago. Loan proposals that once took two days to approve and a short time to transact now require additional documentation including appraisals, environmental assessment reviews and detailed cash flow analyses. Loan approvals take longer and numerous out of pocket costs are borne by the small business borrower. These may well be the same borrowers who have worked with us for years who now have to share with the bank the effect of regulation.

Small banks are limited in the human and technological resources available to meet regulatory requirements, yet we are subject to the same requirements as the largest banks. We are forced to use outside sources because of lack of expertise in reading and interpreting regulations and time restrictions Boilerplate solutions to compliance is not always a good solution, but many small banks have few alternatives

ECONOMIC GROWTH AND FINANCIAL INSTITUTIONS REGULATORY PAPERWORK REDUCTION ACT OF 1993

The Bacchus/Bereuter Bill contains numerous provisions which will help to relieve some of the unnecessary burden of compliance. Each regulation and policy statement which has been adopted in the past few years had its advocates with reason to believe that a problem needed correction. Each, however, has added another layer to the point of overwhelming small banks. None of the provisions of this bill, considered individually, will solve the small banks' dilemma. Each provision does, however, begin to peel away at some of the layers. This bill is an excellent start in rethinking bank regulation and determining which regulations are effective and needed, and which are duplicative, overly complex, and even counterproductive.

I will address a few of the specific areas addressed in H. R. 962 and how they might affect Riverside Bank.

Title II - Regulatory Micromanagement

In the past two years, the Riverside Bank Board of Directors has adopted twelve new policies affecting lending, investment, management, and deposits. Each of these policies was implemented after a new regulation or policy statement was issued by our regulatory agency, the FDIC. Several of these twelve new policies replaced an existing policy but significant changes were required to comply with precise and often detailed requirements.

The new policies adopted are:

1. Real Estate Appraisals
2. Brokered Deposits
3. Branch Closing
4. Interbank Liabilities
5. Prudent Real Estate Lending Standards
6. Environmental Risk
7. Loans to Insiders
8. Other Real Estate Owned and In-Substance Foreclosures
9. Selection of Securities Dealers
10. Prudent Investment Strategy
11. Assets Held for Sale
12. Truth in Savings

We are also anticipating the need to develop three addition policies in the near future:

1. Large Value Funds Transfer
2. EFT Network Service Risks
3. Criminal Referral

We have also, I must admit, been permitted to allow one policy to lapse: Highly Leveraged Loan Transactions. The regulators apparently discovered that the policy was not needed because banks were monitoring their loans adequately.

I cannot unilaterally say that these policies are unnecessary or lacking in any benefit to the bank. Many of them, however, have been adopted only to satisfy regulatory requirements and include sections that have no application to a bank of our size and market The Prudent Real Estate Lending standards policy includes a description of how we would monitor and value a multi-phase development project that we would never enter into anyway, and the Prudent Investment Strategy policy addresses mortgage backed derivative investments that we have never considered purchasing. Requiring banks to have written policies to guide the officers in managing deposits loans and investments is prudent. It is not possible, though, to mandate the details of those policies in a way that will be equally meaningful and beneficial for banks from $25 million to several billion in size Many factors influence bank s management, from size, location and market area to its earnings history lending philosophy and capital strength. Each bank must be given latitude to develop policies that benefit them and their own communities The examination process is thorough enough to allow the regulators the opportunity to converse with bank management about the adequacy of their policies and to require any needed changes.

Policy mandates frequently require the bank to monitor the level of activity or volumes of certain transactions, such as loans over a certain loan-to-value ratio We are seeing a trend towards artificial ceilings on activities, based on aggregate totals with no regard for the individual transaction. We are particularly concerned at Riverside Bank about the affects of the Real Estate Lending standards. Because of our size, just a few sizable loans for community development projects could cause us to exceed the 30% of capital benchmark and cut off additional funds for these projects. This is a good example of a rigid policy requirement that does not take into consideration the ability of the bank s officers and directors to make well-considered lending decisions.

All of the current policy requirements pale beside the requirements of Section 132 of FDICIA regarding standards on bank operating procedures. If it is difficult to prescribe standards for real estate lending, it will be impossible to develop any meaningful standards for operating procedures. Banks are as much different from each other as they are the same.

While I appreciate the proposed exemption of well-capitalized and well-managed banks, I do not expect this to be a worthwhile effort for any group of banks.

Implementation Pressure

It has been a time-consuming effort to keep up with the volume of new and amended regulations in the past few years. This has been especially difficult because of the unreasonably short time periods allowed in many cases. We rely on the FDIC to inform us of changes and new requirements. The FDIC's communications department distributes policy statements, regulations and other materials to banks shortly after they are published in the Federal Register. I would like to describe three recent requirements for which we had extremely short time periods to comply.

1. Policy on Selecting Securities Dealers and Prudent Investment Strategies

   FDIC release date 1-17-92
   Effective date 2-10-92

2. Policy on Prudent Real Estate Lending Standards

   FDIC release date 1-12-93
   Effective date 3-19-93

3. Regulation F, Interbank Liabilities

   FDIC release date 2-05-93
   Effective date 6-19-93

Note that not only are these time periods for developing and implementing new policies and procedures very short, they may occur at the same time, which requires quick action on multiple projects at the bank. These often involve the same people at our bank with 14 officers. The short time frames pressure us to rush the policy, often without having completely discussed its effects or thoroughly trained our staff. A longer preparation time would result in better policies because of the opportunity to involve additional people in the discussion and the time allowed to explore the capabilities of our systems and operations.

Title III - Unnecessary Cost, Paperwork and Regulation

The Branch Closing requirements were newly adopted in 1992 when we moved one of our three branch offices one mile down the same street. We were required to mail notices, post a notice, provide reasons to the FDIC, and wait 90 days before moving. All this was required for a move that was done to make us more convenient and accessible to most of our customers.

Title IV - Consumer Inconvenience, Paperwork and Cost

Many regulations which were enacted to provide consumers with information with which to make informed choices do not accomplish this goal and sometimes are actually counterproductive. The worst example, as I am sure you have heard before, is in home lending with adjustable rate mortgages. An applicant for such a loan is subject to at least ten separate disclosure provisions, each with their own mandated language and format and different timing requirements. We have procedures in place to ensure that we comply with these ten provisions, but I doubt that the ultimate goal of borrower awareness and understanding is accomplished. There are other examples in consumer and mortgage lending of regulations which have been issued at different times, and by different agencies, which do not work together to accomplish their objectives.

Many banks of similar size to Riverside Bank elect not to offer certain kinds of credit products, particularly adjustable rate mortgages and home equity lines of credit. Because we are located in a large metropolitan area we cannot make that choice and remain competitive. We have therefore invested in computer software to produce the proper disclosures and other documents. We recently purchased a new program for home equity lines of credit for $4,000 - we have a total of 166 of these loans at this time. That is $24 per loan just for the disclosure software.

There are numerous logical ways to streamline the application and lending process that will benefit not only banks but also borrowers The consumers right to rescind second mortgages is meant to protect consumers but actually causes them inconvenience, which they blame on the bank. In my eleven years involved in lending I have not seen a single transaction rescinded and have allowed only three waivers of the right to rescind.

Recent changes to RESPA expanded coverage to loans made for business purposes. I urge you to exempt business and agricultural loans from this coverage. We have already found that the disclosures required for compliance serve no purpose except compliance for its own sake. A recent business line of credit, for example, was guaranteed by the two business owners. They each secured their guarantees with mortgages on their home which they own free and clear. We were required under RESPA to provide them with early disclosures about transferring servicing rights and closing costs, and with a settlement statement at closing which contained only two entries RESPA is a regulation for consumer home mortgages and has no benefits for business borrowers.

TITLE V - COMMUNITY REINVESTMENT

The last title of the bill affects the Community Reinvestment Act. I understand that some of these provisions have been superceded by President Clinton's actions with the regulatory agencies, but I want to comment briefly on CRA compliance.

Riverside Bank is proud to have received Outstanding CRA ratings from the FDIC in both 1992 and 1993. We believe that this rating recognizes our active participation in community development and small business lending in Minneapolis. Local government and media have praised Riverside's willingness to go the extra mile to make projects work that might have languished if we only made "cookie cutter" type loans. These loans are not made because of CRA - we would have made them before 1990 or before 1977. We make them because we believe they are good loans.

Our outstanding ratings might, however, be more a reflection of our detailed documentation and computer reports. Our twelve calling officers have met with 52 different groups in the last year and completed approximately 160 written forms to prove that they met. We will spend $3000 each year on computer generated color maps to prove that we make loans in Minneapolis. We will continue to spend time and other resources documenting our performance, lessening the time and resources available to actually perform. Any relief from these paperwork burdens will enable us to dedicate these resources as they should be.

CONCLUSION

Mr. Chairman, as a compliance professional I will continue to develop policies and procedures and train our staff to comply with whatever regulations are implemented that affect our banking activities. At the front lines, however, we know that many of these regulations could be modified to lessen the burden while still achieving, or even improving upon, the ultimate goal of consumer protections and bank safety and soundness. I appreciate the invitation to appear today and share my experiences as they relate to the proposed legislation. Thank you.

Statement of

STEPHEN A. KASE
GENERAL COUNSEL AND COMPLIANCE OFFICER
BANK OF STURGEON BAY, STURGEON BAY, WISCONSIN

before the

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS SUPERVISION, REGULATION AND DEPOSIT INSURANCE

of the

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

UNITED STATES HOUSE OF REPRESENTATIVES

September 23, 1993

Mr. Chairman, I am Stephen Kase, General Counsel and Compliance Officer for Bank of Sturgeon Bay, a Wisconsin state chartered member bank of the Federal Reserve System. Bank of Sturgeon Bay is a 100 year old community bank of slightly over $200 Million in assets, located in Sturgeon Bay, Wisconsin. Sturgeon Bay is a city of 10,000 centered in a rural county of about 25,000 northeast of Green Bay.

I have been in the banking profession for the past thirteen years, all of those with my present bank. Though I carry out a variety of duties including that of compliance, I have watched that particular aspect of my job grow monumentally during that time. In my capacity as the bank's Compliance Officer, I am tasked with responsibility for education, training, and implementation for federal and state banking regulation as well as numerous additional non-banking regulations which affect our operation and activities.

I am honored to appear before this subcommittee today to present testimony in support of the Economic Growth and Financial Institutions Regulatory Paperwork Reduction Act (H.R. 962). I do so with the distinct perspective of the rural small town community bank. It is a perspective of which I am proud and one which I hope merits your attention in considering the impact of this legislation on the future of banking in America.

STATEMENT OF PURPOSE.

As a nation, we have fostered a proud tradition of protection for those who cannot protect themselves. Laws are established to direct our behavior and guide our activities. Banking regulation, at its best, adheres to this concept. It maintains the safety and soundness of financial institutions. It provides a level playing field for the consumer, ensuring fair and equal access to banking services. Most importantly, its continuing presence promotes community and national values.

It can be argued that every law, every regulation has a valid purpose. Each new regulation is introduced to correct some inequity or "right a wrong". However, the effect of such laws and regulations is sometimes not anticipated. The cost of regulation may simply exceed the economic benefit of compliance. In that event, the long term effect of regulation may work against the people it was intended to protect.

In the Sturgeon Bay community, the expressions of concern about banking regulation take on a different meaning. My bank supports regulatory supervision as a necessary part of banking activity. It does not dispute the need for sound operation and consumer protection. We do our best to support our customers and our community.

However, we do not experience complaints about our compliance efforts. Instead, we hear objections about excessive interference from government regulation. These objections result from the volume and incomprehensibility of disclosure documents. Therefore, much of what is required to do to protect the public and protect us from ourselves, so to speak, appears unnecessary. That is where we become concerned about "regulatory burden."

We question the value of these so-called "protective" laws when the only apparent result is increased costs for documentation and disclosure. Such laws have placed burdens on banks not equally applied to its competitors. They have affected the ability of financial institutions to compete and encouraged a massive shift of assets away from the financial industry to other less regulated avenues of investment.

From our point of view, "regulatory burden" can be defined by the following: it requires costly records and statistics to prove compliance; it concentrates on the "letter" of the law and ignores the "spirit"; and it imposes penalties without room for innocent mistake or personal judgment by the examiners.

REGULATORY COSTS.

Bank of Sturgeon Bay has always attempted to provide the widest possible range of credit and deposit products. However, as the direct result of increasing regulatory pressure, we have been forced to limit products and services which might otherwise have been available to our customers. Most prominently, we do not offer adjustable rate mortgages due to the complicated disclosure requirements of Truth in Lending.

These decisions were ultimately made based upon regulatory rather than economic considerations. As an unsophisticated community bank, it was simpler to limit our services than to deal with the cost of expanded regulatory compliance. In the end, every product we offer carries a compliance cost and those costs must be included in each product we make available to our customers.

To demonstrate the financial impact, I have attached a limited regulatory cost survey of six prominent regulations and our compliance management program. The costs incurred relate solely to compliance activity, not to issues of safety and soundness. While there are numerous other regulations of lesser impact, these are representative to show part of the high cost of compliance.

We carry a heavy cost to demonstrate compliance with these regulations. The end result is increased time, expanded documentation, and higher cost of services. Even as every business must absorb and deal with the cost of its services, those costs must be shared. They inevitably result in reduced profits and increased costs to the consumer.

DISCUSSION.

Given the limitations of time, I cannot begin to address all of the aspects of this legislation. In addition, my expertise is certainly not sufficient to advise this subcommittee on many of the detailed technical aspects involved. I will not expound on generalities or recite industry facts and figures. My voice will not sway your opinion on those matters. However, detailed testimony about the direct real life impact of this bill is worthwhile. Each of the sections of this bill represents a concern of one or more segments of our banking community.

Rather, I believe it will be productive to focus on several sections of particular importance to our bank and perhaps to other banks in similar circumstances. Hopefully, others will fill in the gaps and in the end, you will have a comprehensive range of testimony from which to make your decisions.

You are no doubt aware that there are different aspects of "regulatory burden". First, certain regulations are appropriate to some situations, but not to others. A great portion of FDICIA burdens fall into this category. Motivated by concerns about troubled banks, rules were applied equally to all banks. Second, there is duplication of disclosure requirements. By example, it has been suggested that the RESPA rules cross lines of disclosure with Truth in Lending. Third, there is regulatory overkill, situations in which the degree of regulation far exceeds the need. Much of the concern expressed about CRA is not the motivation to meet community credit needs, but the massive record keeping to "demonstrate" compliance.

The proposals I will discuss touch on all three of these issues. They are ones which, if incorporated into law, would have the most beneficial effect on my bank and my job. They range from authorizing studies and reports for further consideration down to immediate and significant relief in the day to day functioning of banking compliance. In every case they will save hours and dollars for my bank, yet in no case will they affect the safety and soundness of my institution or increase any risk to our customers.

SEC 122. CULPABILITY STANDARDS FOR OUTSIDE DIRECTORS. [Page 13]

FDIC amended to modify potential liability against outside directors, changing their classification concerning imposition of monetary penalties.

The thorny issue of management responsibility must be approached with great care. It strikes at the very heart of many perceived problems addressed by FIRREA and FDICIA legislation. Yet at the same time, the standards by which directors are held accountable must bear a reasonable relationship to their degree of involvement. The proposed amendment addresses the recognized difference between the "outside" and "inside" director.

The "inside" director becomes a part of the functioning management team. However, the "outside" director is often chosen for other reasons. Their skills and judgments are needed for balance, perspective, and objective guidance of the bank's activities.

In the context of the rural community bank, we face a difficult challenge identifying women and men who can contribute and are willing to serve. The expectation of a sophisticated and experienced board of directors, all fully knowledgeable about the operation of modern banking, is unrealistic. While some directors may become involved in inside management, others do not. Their participation is based on recognition of the need for community involvement. Thus, the very goals served under regulations such as CRA and ECOA potentially place directors at high risk for their willingness to serve.

We consider Section 122 to be highly supportive of community involvement without reducing the level of responsibility assessed upon those who willingly enter into the inner circle of bank management and control.

SEC 201. REGULATORY STANDARDS. [Page 22]

FDIC (FDICIA of 1991) amended to provide an exemption from prescribed operating standards for properly managed banks (CAMEL 1 or 2).

SEC 202. PAPERWORK REDUCTION REVIEW. [Page 24]

Regulatory agencies to report on "unnecessary internal written policies" for purposes of elimination of such requirements.

Among the fundamental purposes of FDICIA was the protection of financial institutions against failure through improper management. Among other things, great attention was directed toward practices and policies to direct troubled institutions toward recovery. One unfortunate consequence of this Act was that those institutions which were not troubled, which were well managed have been burdened with the massive rewriting of internal policies and procedures. It was not that these institutions didn't properly deal with the issues addressed by the Act, only that they did not deal with them in the manner now required by law.

It makes sense to apply corrective action to those institutions which need it, but this amendment recognizes that those institutions already doing their job well do not need the increased regulatory scrutiny and interference created by mandatory structured policies set forth under FDICIA operating standards.

The focus of corrective action should be on troubled institutions. If the patient is examined and found healthy, what's the sense of prescribing expensive and unpleasant medicine? These amendments appear to recognize that premise. They will not reduce the attention directed to institutions that need it, but relieve some of the burden now imposed on those that don't.

SEC 301. ANNUAL EXAMINATIONS. [Page 25]

FDIC (FDICIA of 1991) amended: For bank of less than $250 Million, well capitalized, well managed banks in compliance with federal regulations may be examined every 2 years. In addition, applicable state examinations may satisfy federal examination requirements. Rule may be extended to holding companies within scope of principal bank examination.

In considering the impact of government regulation, the examination process creates a significant disruption of banking operations. Among the most desirable elements of this legislation is the recognition of sound community banks with respect to the burden of regulatory examination.

My bank is the sole subsidiary of a bank holding company. We must be prepared for examination of the holding company as well as multiple examinations of our subsidiary bank by both state and federal regulators for safety & soundness and regulatory compliance. This has resulted in as many as four distinct examinations within a single year.

There is duplication of effort, at least between state and federal regulators. Though the condition of the bank remains essentially unchanged during that short period of time, regulators are required to separately evaluate essentially the same fundamental concerns.

The proposal suggests that where a bank demonstrates adequate performance under federal safety and soundness guidelines, then the examination requirements can be adjusted accordingly. The cost savings is obvious, both to the bank and the regulatory agency. Of even greater importance is that critical resources can be more effectively directed toward scrutiny of those institutions which do not satisfy regulatory standards.

At a time when there are almost insurmountable demands upon the resources of government, regulators can rely on the proved performance of successful financial institutions and focus attention where it is needed most.

SEC 307. BANK SECRECY ACT AMENDMENTS. [Page 37]

> **31 USC amended: Introduction of annual report of written rulings, reduction of "Cash Log" requirements for transactions by identified customers, shifted burden to customer for filing of CTR, and inflation adjustment for CTR filing amounts.**

Among the most significant improvements proposed in this bill are the changes to Bank Secrecy Act record keeping requirements. I can assure you that our bank takes its responsibilities under this act very seriously. However, these records are highly detailed and there are serious penalties for error. Fear of making a mistake and greater fear of the possible consequences sometimes actually overshadow the underlying regulatory purpose.

Identification procedures remain in place. One change simply reduces the unnecessary recording of non-reportable transactions by identified bank customers, a second allows for minor adjustments to match inflation. The third transfers responsibility for cash transaction reporting from the bank to the customer. Reporting and identification requirements remain intact.

I understand you have heard testimony against this proposal. I would only offer that nothing in the act lessens the accuracy of the information to be gathered, nothing reduces the transactions to be reported. The amendment merely recognizes that the customer is the one who best knows the information and places responsibility for accurate reporting properly on the one who benefits instead of on the innocent employee who merely accepts the transaction.

SEC 401. STREAMLINED LENDING FOR CONSUMER BENEFIT. [Page 49]

Federal Reserve System report concerning ways to streamline consumer lending, implement simplifications and report on recommendations for legislative changes.

I need not spend much time endorsing this proposal. Albeit there is an obligation imposed on our regulators, but I believe it is one which will lead to benefits for all concerned. If there is one universal comment we have heard increasingly over recent years, it is this. "The sheer waste of time, money, and resources expended on undesired consumer disclosure is an outrage!"

While not questioning the sincerity of consumer advocates who speak for more stringent and expansive rules, I wonder at the opinion of many thousands of banking customers who continue to be frustrated, confused, and downright angry about the morass of paperwork they must wade through. I must state anecdotally that not once in my thirteen years in compliance has a consumer ever expressed satisfaction or appreciation at the hoops they must jump through or the disclosures they must try to understand.

SEC 406. ELIMINATION OF DISCLOSURES FOR EQUITY LOANS. [Page 52]

RESPA amended to provide that in the case of Home Equity Loans, existing TIL disclosure would satisfy requirements.

SEC 442. EXEMPTION OF BUSINESS LOANS. [Page 58]

RESPA amended to provide exemption from disclosure for business, commercial, or agricultural and refinancings involving 25 acres or more.

I have identified these two proposals as representative of the very worst problems our bank faces with the new improved RESPA. Not even a year ago, RESPA was one of the simplest and well followed regulations in our lending area. It made sense, it was well intentioned, and our lenders believed in its value. Yet we now face a situation in which the important, but narrow problems addressed in the changes has been completely obscured by the massive overkill which resulted.

The first amendment would recognize that the extensive Truth in Lending disclosure for Home Equity Loans has done its job. Existing TIL disclosures more than adequately advise the consumer of important loan information. RESPA now requires duplication of much of that disclosure over again merely in different format. Similarly, as to the second proposal, consider how remote from its original intention that RESPA requires disclosure to a business on a commercial loan merely if it happens to offer residential property as collateral. These changes only attempt to redirect RESPA toward its original purpose: to ensure that real people get real disclosure information when putting their homes at risk.

SEC 501. COMMUNITY REINVESTMENT ACT AMENDMENTS. [Page 59]

CRA amended: Safe Harbor protection for "outstanding" rating regarding applications, credit for "incentive" lending, the recognition of "special purpose" banks, and acceptance of equivalent state examinations for CRA compliance.

Among the most controversial element of the recent regulatory activity has been the implementation of new CRA guidelines. Perhaps more than any other regulation, the Community Reinvestment Act can be said to epitomize the debate about regulatory burden.

I am a strong supporter of CRA and I believe we can all agree that community reinvestment is a good idea. In a sense, it goes to the very heart of community banking, reinforcing the partnership between the bank and the community it serves. On its face, the mere 6 pages of the CRA regulation does not seem burdensome. The examination process asks banks to show what they do, not do more than they should.

However, the implementation of examination standards have created a regulatory nightmare. Financial institutions are buried in a morass of useless paper, regulatory agencies struggle with problems of enforcement, and consumer advocates assert that the Act has failed to do its job.

The amendment proposes to reduce paperwork, establish a "safe harbor" for institutions rated Outstanding, give credit for special lending initiatives, clarify the responsibilities of special purpose banks, and eliminate redundant examinations. They should not raise concerns about CRA effectiveness. They would reward banks that fulfill their responsibilities, provide clearer guidelines for identifying valid CRA initiatives, and reduce the duplication of effort in states recognized as having equivalent laws for community reinvestment.

These are not bad things. The amendments do not suggest a reduction of effort. They do not undermine the essential purposes of the Act. Rather, they provide clearer direction to banks seeking to comply with the law and such measures should be encouraged.

CONCLUSION.

I agree that laws should be adopted to correct problems in our industry. I also agree that these laws should not be tinkered with in a cavalier manner. However, the proposals before you in this bill meet both tests. The problem of regulatory burden is as real to us as you could possibly imagine and we need your help.

At the same time, these amendments alleviate burdens for the well run, successful bank without lessening the safety and soundness protections which underlay our regulatory system. I hope that the impact of a "Reduction Act" will be focused on clearly defined and obtainable objectives. The best objectives are those which let us operate freely to serve our communities.

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- Reduce the dollar cost of compliance activity.
- Reduce the complexity of technical requirements and the time necessary for compliance.
- Reduce automatic penalties and let the examiners identify problems and determine the solution.
- Expand opportunities for lending activity, incentives, remove disincentives.

I have attempted during this time to advise you of various aspects of H.R. 962 which would have a positive impact on my own bank's activities. However, I think it appropriate to leave you with a brief priority list of initiatives considered most beneficial.

Section 301 - Annual Examination. The out of pocket costs of preparing for and going through regulatory examinations are substantial. Based upon strong performance and a satisfactory compliance record, simultaneous annual state and federal exams directed toward the same purpose would be eliminated. The cost savings, both for banks and regulatory agencies would be substantial. The savings could be properly channeled toward those institutions most in need of supervision and examination.

Sections 210 and 202 - Exemption from prescribed standards and specific written policies. Although defined operating standards and written policies are essential, these two amendments would give recognition to banks that already have appropriate standards and policies in place. We would benefit substantially by continuing to utilize successful existing policies and procedures and avoid "reinventing the wheel" simply to meet regulatory specifications.

Sections 406 and 442 - RESPA Amendments. These two amendments would go far in reasserting the original principles of RESPA protecting the family home. For our bank, these changes would reduce almost by half the unnecessary RESPA disclosure to those who either are not pledging their homes or who are already receiving extensive disclosure and rescission rights under Truth in Lending.

Section 501 - CRA amendments. CRA is a critical weapon in the struggle to combat discriminatory lending practices and direct financial resources into local communities. However, we must allow the system to work. The amendment would simplify the ability of banks to meet CRA expectations. When financial institutions demonstrate pro-active CRA support with a rating of "Outstanding", this amendment would credit that effort, reduce their cost of compliance, and direct critical resources toward institutions that do not meet community reinvestment responsibilities.

CONCLUSION.

Congress faces a monumental task in overseeing the welfare of the country. The importance and complexity of the issues are staggering. This bill may easily be overshadowed by problems of far greater significance. However, in your deliberations, I urge you to recognize their importance to the banking industry and to banks like mine.

Banking regulation must benefit banking if it is to ultimately benefit the community. Fair regulations guide the banking profession and protect the people. Unfair and burdensome regulations offer no guidance and protect noone. The impact of excessive regulation is to punish the customer through higher costs and reduced availability of banking services.

It is no longer a question of doing our job, but of facing ever increasing difficulty in demonstrating that we are doing it right. Every new increase in regulatory obligations increases the complexity and cost of banking activity. No single piece of legislation makes or breaks the system, but at some point, the small community bank will no longer be able to cope.

Many have already decided it is easier to sell out, passing the burden on to regional or national banks better able to meet the awesome task of regulatory compliance. When that happens, we must question whether the consumer is better off without access to a locally owned and locally dedicated financial institution!

Give careful consideration to the impact of regulatory burden on the community bank; small independent banks like mine which have existed for decades providing essential financial services to millions of people in this nation. For us, serving the community is a way of life. We live and work alongside our customers every day. We are fair and open in our dealings. We do our very best to help our community. In the end, their success is our success.

In closing, I sincerely commend the authors and collaborators on this bill for recognizing numerous opportunities to improve banking regulation. It offers you the chance to recognize the effort and value of community banks. Seize this opportunity to support healthy and economically sound local financial institutions. Help us to meet local credit needs and make banking services more affordable to the consumer.

Statement of Stephen A. Kase
Exhibit "A" September 23, 1993

REGULATORY COST SURVEY

This analysis addresses the costs of regulatory compliance. Information presented in this analysis is not submitted with fundamental objection to the purposes or goals of legitimate banking regulation. Rather, it is intended as a basic cost estimate, primarily directed toward enlightening the reader about the significant cost of performance of regulatory activities.

The survey was accomplished through basic calculations supported by wage and salary averages, cost of supplies and training, and conservative estimates of hours involved in compliance activity. It incorporates statistical information about selected major regulations not addressing the safety and soundness of banking activity and offers reliable quantitative data relating to the costs and time attributable to regulatory compliance.

It should be noted that this institutions remains subject to numerous other laws and regulations of varying impact and burden such as the Americans with Disabilities Act (ADA), Equal Employment Opportunity Commission (EEOC) regulations, the Fair Debt Collection Act (FDCA), the Fair Credit Reporting Act (FCRA), the Right to Financial Privacy Act (RFPA), Occupational Safety Hazards Act (OSHA) and other federal and state laws and regulations affecting the cost of bank operations and services. However, with regard to examining the burden of governmental regulation of banking, it is suggested that the regulations and laws reviewed in this analysis identify a recognizable point of departure for corrective action.

I. BACKGROUND.

The regulations selected for evaluation, although significant in impact and familiar to the public, do not deal with matters ensuring the safety and soundness of bank operation. Most, although not all, are generally considered to be "Consumer" regulations. The others reflect the increasing demands of government to assist in the record keeping process related to taxation and crime.

Regulations were evaluated for direct costs (regulatory activity) and indirect costs (documentation, training, and verification). Only regulatory functions were counted (ie. documentation was divided between preparation regulatory disclosure vs. standard loan notes and security agreements). Similarly, employee hours were calculated solely upon the compliance activity involved exclude non-regulatory banking functions. Hard costs, including forms and reports were charged only when dedicated to compliance activity. Calculations were based upon documentation of transactions and accounts. Cost formulas multiplied estimates of employee time per transaction by number of transactions involved. Transaction estimates are based on 1993 banking activity.

The total cost incurred for compliance with the six regulations and the compliance management program is $212,777 in wages and hard costs.

II. COST AREAS FOR CALCULATION OF REGULATORY BURDEN.

A. JOB PERFORMANCE. Brief description of the functions required under the regulation and time expended on an annual basis.

B. DOCUMENTATION & RECORD KEEPING. Specific records and recording activities involved in documenting regulatory compliance.

C. FORMS, NOTICES, AND DISCLOSURES. Written documents expressly required by regulations which must be produced and delivered under compliance requirements.

D. REVIEW, AUDIT & ACCOUNTING. Activities involved in the verification of accurate and complete regulatory performance.

E. MANAGEMENT REVIEW AND SUPERVISION. Activities involved in managerial organization, implementation, and oversight of the bank's regulatory compliance program.

1. PROGRAM SUPERVISION. Specific activities of persons delegated responsibility for directing the compliance program.

2. MANAGEMENT COMMITTEES. Management level review of regulatory compliance matters and performance.

3. DIRECTOR COMMITTEES. Upper management and board of directors level review of regulatory compliance matters and performance.

F. EDUCATION & TRAINING. General activities related to preparing employees to understand regulatory requirements and perform compliance activities.

1. EDUCATION. Outside schooling on regulatory and compliance matters.

2. RESOURCE MATERIALS. Outside publications purchased to augment internal resources for compliance activities.

3. EMPLOYEE HOURS. Time committed by employees to outside seminars and internal training sessions.

G. COMPLIANCE EXAMINATIONS. Costs incurred by the bank imposed by the regulatory system to verify bank performance in regulatory areas reviewed in this analysis. The cost is identified in employee hours expended in preparation for and assistance during the compliance examination.

TITLE:	TRUTH IN SAVINGS					
				HRS	WAGE	DOLLARS
A. JOB PERFORMANCE		TIME	TRANS			
	NEW ACCT DISCLOSURES	.05	7320	366	11.06	$4,048
B. DOCUMENTATION & RECORDKEEPING		HOURS	MONTHS			
	INTEREST DISCLOSURE RECORDS	2	12	24	11.06	$265
C. FORMS, NOTICES, AND DISCLOSURES		PRICE	NUMBER			
	DISCLOSURE FORMS	0.25	7320			$1,830
D. REVIEW AND AUDIT		HOURS	MONTHS			
	PRODUCT MARKETING REVIEW	2	12	24	42.16	$1,012
	ADVERTISING REVIEW	5	12	60	9.11	$547
	COMPLIANCE VERIFICATION	2	12	24	40.16	$964
	INTERNAL AUDIT	48	2	96	9.32	$895
				594		$9,561

TITLE:	COMMUNITY REINVESTMENT ACT					
A. JOB PERFORMANCE		TIME	TRANS	HRS	WAGE	DOLLARS
	OFFICER CALL PROGRAM	0.2	480	96	25	$2,400
	CRA LOAN IDENTIFICATION	0.1	375	38	25	$950
	STAFF CRA LOAN REPORTING	0.1	375	38	10.20	$388
B. DOCUMENTATION & RECORDKEEPING		HOURS	MONTHS			
	CRA LOAN REPORT	1	12	12	9.11	$109
	EMPLOYEE CRA SURVEY	60	1	60	22	$1,320
	CRA OFFICER ACTIVITY	25	12	300	42.16	$12,648
	CRA STAFF ACTIVITY	30	12	360	9.45	$3,402
	CRA COMMITTEE ACTIVITY	9	6	54	42.16	$2,277
C. FORMS, NOTICES, AND DISCLOSURES		PRICE	NUMBER			NONE
D. REVIEW AND AUDIT		HOURS	MONTHS			
	ANNUAL CRA REPORTS	60	1	60	56	$3,360
	BOARD OF DIRECTORS REPORT	4.5	12	54	56	$3,024
	INTERNAL AUDIT	15	2	30	9.32	$280
				1,102		$30,158

TITLE:	TRUTH IN LENDING							
						HRS	WAGE	DOLLARS
A. JOB PERFORMANCE				TIME	TRANS			
	LOAN OFFICER DISCLOSURES			0.3	1219	366	25	$9,150
	STAFF DOCUMENT PREPARATION			0.4	1219	488	9.89	$4,826
	COMPLIANCE SCREENING			0.2	1219	244	9.11	$2,223
	DELINQUENCY NOTICES			0.4	100	40	9.11	$364
B. DOCUMENTATION & RECORDKEEPING				HOURS	MONTHS			
	FILE MAINTENANCE			30	12	360	8.78	$3,161
	ANNUAL DISCLOSURE NOTICES			15	1	15	9.11	$137
C. FORMS, NOTICES, AND DISCLOSURES				PRICE	NUMBER			
	DISCLOSURE FORMS			0.15	5991			$899
D. REVIEW AND AUDIT				HOURS	MONTHS			
	STAFF FILE REVIEW			175	12	2,100	9.11	$19,131
	INTERNAL AUDIT			15	12	180	9.32	$1,678
						3,793		$41,569

TITLE:	R.E.S.P.A. ACT							
						HRS	WAGE	DOLLARS
A. JOB PERFORMANCE				TIME	TRANS			
	LOAN DISCLOSURES			0.2	750	150	25	$3,750
	STAFF RESPA DOCUMENT PREP			0.4	750	300	9.89	$2,967
B. DOCUMENTATION & RECORDKEEPING				HOURS	MONTHS			
	FILE MAINTENANCE			2	12	24	9.89	$237
C. FORMS, NOTICES, AND DISCLOSURES				PRICE	NUMBER			NO COST
D. REVIEW AND AUDIT				HOURS	MONTHS			
	STAFF FILE REVIEW			2	12	24	9.11	$219
	INTERNAL AUDIT			15	2	30	9.32	$280
						528		$7,453

TITLE:	BANK SECRECY ACT					
				HRS	WAGE	DOLLARS
A. JOB PERFORMANCE		TIME	TRANS			
	CTR REPORTING	0.2	275	55	9.17	$504
	MONETARY INSTRUMENT LOGS	0.5	480	240	9.17	$2,201
	CURRENCY TRANS LOGS	0.03	47920	1,438	9.17	$13,186
	EXEMPTION VERIFICATIONS	0.03	1500	45	9.17	$413
	IRS TRANSACTION INQUIRIES	0.4	25	10	56	$560
B. DOCUMENTATION & RECORDKEEPING		HOURS	MONTHS			
	RECORDS MAINTENANCE	10	12	120	9.45	$1,134
	DISCREPANCY REPORTS	18	12	216	9.45	$2,041
	EXEMPTION MAINTENANCE	25	2	50	9.45	$473
C. FORMS, NOTICES, AND DISCLOSURES		PRICE	NUMBER			
	DOCUMENTATION RECORDS	0.09	2275	205		$205
D. REVIEW AND AUDIT		HOURS	MONTHS			
	CTR & MONETARY VERIFICATION	5	12	60	9.45	$567
	CURRENCY TRANS VERIFICATION	6	12	72	9.45	$680
	EXEMPTION LIST VERIFICATION	40	4	160	9.32	$1,491
	INTERNAL AUDIT	24	4	96	9.32	$895
				2,767		$24,350

TITLE:	DEPOSIT ACCOUNT WITHHOLDING						
A. JOB PERFORMANCE			TIME	TRANS	HRS	WAGE	DOLLARS
	NEW ACCT DISCLOSURE		0.1	5520	552	11.06	$6,105
	WITHHOLDING NOTIFICATIONS		0.3	150	45	9.97	$449
	IRS LEVY PROCESSING		0.6	120	72	9.45	$680
B. DOCUMENTATION & RECORDKEEPING			HOURS	MONTHS			
	RECORDS MAINTENANCE		3	12	36	9.45	$340
	ANNUAL REPORTING		60	1	60	56	$3,360
	IRS LEVY REPORTING		9	12	108	9.45	$1,021
C. FORMS, NOTICES, AND DISCLOSURES			PRICE	NUMBER			NO COST
D. REVIEW AND AUDIT			HOURS	MONTHS			
	INTERNAL AUDIT		30	2	60	9.32	$559
TOTAL					933		$12,514

TITLE:	COMPLIANCE MANAGEMENT							
						HRS	WAGE	DOLLA RS
E. MANAGEMENT REVIEW & SUPERVISION				HOURS	MONTHS			
1. PROGRAM SUPERVISION								
	COMPLIANCE MANAGEMENT			60	12	720	45	$32,400
	SYSTEM DOCUMENTATION							
		FILE MAINTENANCE		4	12	48	45	$2,160
		MEMORANDA		4	12	48	45	$2,160
	COMPLIANCE REPORTS							
		DIRECTORS		1	12	12	45	$540
		MANAGEMENT		2	12	24	45	$1,080
	STAFF TRAINING							
		COMPLIANCE STAFF		8	12	96	9.45	$907
		AUDIT STAFF		4	12	48	9.32	$447
2. MANAGEMENT REVIEW								
	OFFICER LOAN COMMITTEE			6	12	72	25	$1,800
	COMPLIANCE COMMITTEE			10	12	120	45	$5,400
3. DIRECTOR COMMITTEE REVIEW								
	AUDIT & LEGAL COMMITTEE			8	12	96	37.5	$3,600
	EXECUTIVE COMMITTEE			4	4	16	37.5	$600
	BD OF DIRECTORS			15	4	60	55	$3,300
F. EDUCATION & TRAINING								
1. ANNUAL SEMINARS AND EDUCATION								
	COMPLIANCE DEPARTMENT							$3,000
	OPERATIONAL DEPARTMENTS							$3,000

2. LIBRARY & RESOURCE MATERIALS								$7,500
3. SELECTED TRAINING COSTS				HOURS	SESSIONS	TOTAL	WAGES	
		MANAGEM'T		20	4	80	55	$4,400
		NEW HIRES		10	12	120	6.40	$768
		REG B		10	4	40	9.17	$367
		REG Z		35	2	70	9.17	$642
		REG BB		40	2	80	8.50	$680
		REG DD		30	4	120	10.44	$1,253
		RESPA		20	2	40	9.42	$377
		BSA		36	3	108	9.17	$990
		IRS		30	1	30	9.17	$275
	COMPLIANCE OFFICER HOURS			1.5	34	51	45	$2,295
G. REGULATORY COMPLIANCE EXAMINATIONS								
	PRE-EXAM PREPARATION							
		MANAGEMENT PREP		50	1	50	56	$2,800
		BANK STAFF		200	1	200	9.17	$1,834
	EXAMINATION ASSISTANCE							
		MANAGEMENT		30	1	30	56	$1,680
		BANK STAFF		100	1	100	9.17	$917
						2,479		$87,172

STATEMENT OF
DIANNE M. LOPEZ

REGARDING

H.R. 962

BEFORE THE

U.S. HOUSE OF REPRESENTATIVES
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
SUPERVISION, REGULATION AND DEPOSIT
INSURANCE OF THE
COMMITTEE ON BANKING, FINANCE AND
URBAN AFFAIRS

SEPTEMBER 23, 1993

Mr. Chairman and Members of the Committee, my name is Dianne Lopez. I am Senior Vice President and Regional Compliance Manager of First Interstate Bank of Texas N.A. in Houston, Texas. First Interstate Bank of Texas has 93 branches located throughout the state of Texas and has total assets of $5 billion. We are an affiliate of First Interstate Bancorp, a bank holding company owning 17 banks located in 13 states. First Interstate Bancorp is the 13th largest banking organization in the United States with total consolidated assets of $49 5 billion as of June 30, 1993. I am pleased to be here to testify on behalf of First Interstate and am testifying in favor of H.R. 962.

My testimony will focus on Titles II, IV, and V, since these sections will affect the regulations I work with on a daily basis.

Title II

Section 132 of the Federal Deposit Insurance Corporation Improvement Act (FDICIA) requires the bank regulatory agencies to set standards for internal controls and numerous other areas of a bank's day to day operations which affect asset quality. This micro-management by the regulatory agencies is required by FDICIA regardless of a bank's capital level or overall supervisory rating.

These stringent standards will strengthen the regulatory hold that has already been imposed by the savings and loan bail out bill, FIRREA, and could result in banks making fewer loans to new small businesses for fear of violating these rigorous controls on asset quality.

These controls should not apply to institutions that are adequately capitalized with a CAMEL rating of 1 or 2.

Title IV

Currently the Truth in Lending Act requires an incredible amount of disclosure both at the time of application and upon each adjustment to the interest rate I have brought samples of these disclosures for your review today. The disclosures are so onerous that this bank has not been able to operationally comply with the requirements since our conversion to a national bank charter in 1988 and therefore did not offer this product to our customers until March of this year The ARM disclosures are so voluminous that they may in fact be confusing to the borrower This bill would permit lenders to disclose either a history of the index to which the loan will be tied or a statement that the monthly payment may substantially increase or decrease over the life

of the loan. The cap mandated by the Truth in Lending Act would still be applicable, and of course, would be disclosed to the borrower thus preventing a borrower from unknowingly entering into an adjustable rate mortgage that may eventually become unaffordable.

With respect to the Real Estate Settlement Procedures Act, this bill proposes to clarify that the Truth in Lending disclosures currently being provided to borrowers engaging in home equity and home improvement loans are not required to be duplicated by providing them again in the standard settlement form. This will not only ease the cost of compliance for these types of loans but will cause less confusion for the borrower.

Currently, under the Electronic Fund Transfer Act, a consumer s liability for unauthorized transfers is limited to $50 if the unauthorized transfers are reported within two days of discovery This bill proposes to increase that limit to $500 only in cases where the consumer had written the personal identification number on the access card or if the consumer had stored the identification number with the access device. Keep in mind that unauthorized use of an access card is totally different from unauthorized use of a credit card. A credit card may be stolen and used by anyone, therefore the $50 limit of liability makes good sense as long as the credit card issuer is promptly notified by the consumer that the card has been stolen. However if an access device is stolen it is a worthless piece of plastic unless the thief also has the identification number or word. Why should banks foot the bill for this kind of irresponsibility or negligence? It results in losses and subsequently higher fees for everyone, not just those who were negligent.

The bill also proposes to impose financial responsibility on consumers who do not report unauthorized use of credit cards within 60 days of receiving the statement upon which the unauthorized charges appeared This is particularly reasonable in its time request of 60 days and in the fact that the bill specifies that if the consumer is hospitalized or traveling the 60 day notification requirement does not apply. Again, why should the creditor be liable for a consumer s failure to report unauthorized charges? Prompt reporting of the stolen card enables the creditor to freeze usage of the card.

Section 432 of the Bill addresses Homeownership Debt Counseling Notification. Existing law requires lenders to notify delinquent borrowers within 45 days after the initial loan default that homeowner credit counseling programs are available. The proposed amendment would clarify a current

ambiguity by confirming that failure to timely give the notice would not adversely affect foreclosure proceedings under state law. This clarification is highly desirable for several reasons.

Lenders rarely consider a late payment to be a serious default until it is over 30 days past due. This leaves little time for the lender to contact the borrower, determine the cause for the nonpayment, and obtain payment within the time frame allowed. In most cases, the missed payment was an oversight, was lost in the mail, was a result of the payment check being returned for insufficient funds (often to the surprise and embarrassment of the borrower) or was due to some other reason not evidencing an inability or unwillingness to pay. Regardless, in order to meet the 45 day deadline, the lender is required to send a notice to each delinquent borrower which, in effect reminds the customer of the loan default and urges him/her to consider homeownership credit counseling. (What an embarrassment This letter is accurately perceived by the customer as the first step in the lender's collection process To require the lender to prematurely initiate its collection process at this early stage is inefficient, upsetting to the borrower, and damaging to the good will the lender works so hard to develop with it customers. This certainly is not the intention of the law.

Other reasons for not meeting the 45 day deadline include (i) difficulty in negotiating the terms for and scheduling the closing of a loan renewal upon the maturity of a home improvement loan or other short term home loan and (ii) a bad check given late by a customer in response to a call from the lender which is given to the lender prior to the 45 day deadline but not (returned due to insufficient funds) until after the 45 day deadline.

Other less common but equally compelling "excuses" for missing the 45 day deadline are experienced by lenders in the ordinary course of business despite their following prudent banking practices To allow a subsequent foreclosure action to be attacked and found void because of noncompliance with the 45 day notification rule would be unfair and unnecessarily damaging to home lenders and, ultimately more costly to home borrowers.

Currently the Real Estate Settlement Procedures Act (RESPA) requires banks to provide a disclosure of the percentage of loans for which servicing has been transferred This disclosure must reflect the actual percentage of transferred loans for each of the last 3 years. Therefore, each year, the form must be destroyed, reprinted with the latest year's percentage and distributed out to our 93 offices statewide.

Why not simply require us to disclose to borrowers the fact that the servicing of their loan may be transferred and that they will be promptly notified by us at the time of the transfer before the payment is due to the new servicer? This would serve the same purpose but would be far more efficient.

Next, the bill exempts business and agricultural loans from coverage under RESPA. This would save this bank thousands of dollars a year. Commercial borrowers are more sophisticated than consumers borrowers and closing costs associated with loans for business purposes are not a surprise to the borrower. The business purpose borrower knows that loans secured by dwellings will involve attorney's fees for documentation preparation, appraisals, mortgage insurance, etc. and do not need the preliminary disclosures required by RESPA.

Title V:

This title deals with the Community Reinvestment Act (CRA). The first change to be imposed by this bill would be to reduce the paperwork compliance burdens of CRA. Currently the CRA requires the ascertainment of community credit needs. To receive a satisfactory or better rating, this process must be "continuous" and "ongoing" It has been our experience that community credit needs are mostly static and the time and expense invested to demonstrate our good faith effort at compliance yields little or no new information. It should be acceptable for a bank to have a comprehensive process in place for periodically assessing community credit needs in its delineated communities, such as once every 1 - 2 years. Thus saving time and expense which could be devoted towards more results-oriented activities.

Another paperwork burden of the CRA relates to the constant documentation of our efforts to increase loan penetration in our delineated communities, particularly in low and moderate income areas If the numbers of applications received by a bank from low and moderate income persons is not great enough, the bank will surely be criticized and may even be given a less than satisfactory rating, thus freezing all growth until the next exam. In an innovative strategy intended to increase lending to low and moderate income minority neighborhoods, First Interstate Bank of Texas piloted a pre-approved loan offer during 1992 which was repeated in 1993. As you know, pre-approved loan or credit offers are frequently used by banks to reach more affluent prospects, especially in the area of credit cards. We believe that First Interstate may be the first to use the strategy to reach persons below the median income level.

Our strategy called for selecting low and moderate income census tracts which were predominately minority then using a demographics consultant to determine which tract residents were homeowners. Next, that comprehensive listing was processed by the credit bureau using a moderately strict screening criteria. Of the 4,745 minority neighborhood homeowners screened in our first effort, 1,142 were eligible to receive a pre-approved offer of a $1,500 unsecured home improvement loan. Only 7 accepted our offer. We began calling those who did not respond to our offer to better understand their reasons. Of course, many indicated that they simply did not have a current need, but an equal number indicated that they were averse to credit. In other words, they chose to preserve their good credit profile by not accepting credit unless absolutely necessary.

To determine if our first experience was an aberration, we repeated this effort in 1993 Selecting different census tracts using the same profile, we credit screened 32,125 minority neighborhood homeowners. Of that number, 3,662 were eligible to receive our pre-approved loan offer, but only 11 accepted. A related finding from this process is that in our most recent effort, over 85% of homeowners in these tracts failed the credit screening under the first tier, or the most lenient criteria meaning that the credit record contained numerous derogatory listings.

We believe this experience suggests that it is not a financial institution's unwillingness to extend credit to minorities and lower-income applicants that stands as a barrier to achieving parity in lending rates, but broad-based societal biases which have left these individuals more vulnerable to health and employment crises which may lead to credit-related problems Also a factor is the hesitation to accept credit among those with sound credit ratings.

In light of the above efforts to increase our loan penetration in low and moderate income census tracts, I asked the OCC if we could count these credit offers on our Home Mortgage Disclosure Report and categorize them as withdrawn applications. Their answer was "no". Therefore, our HMDA report continues to reflect rather small numbers of applications from low and moderate income census tracts, even though we advertise in these areas, conduct workshops, actively participate in the communities, and offered pre-approved loans.

I thank the Chairman and members of the Committee for the opportunity to speak today and I would be happy to answer any questions.

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TESTIMONY ON REGULATORY BURDEN RELIEF

H.R. 962

GIVEN BY

JAMES A. HANSEN
DIRECTOR OF BANKING AND FINANCE
STATE OF NEBRASKA

AND

VICE CHAIRMAN
CONFERENCE OF STATE BANK SUPERVISORS

BEFORE THE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS SUPERVISION,
REGULATION AND DEPOSIT INSURANCE

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

U.S. HOUSE OF REPRESENTATIVES

SEPTEMBER 23, 1993

Chairman Neal, Mr. McCollum, and Members of the Committee, my name is Jim Hansen. I am the Director of Banking and Finance for the State of Nebraska and Vice Chairman of the Conference of State Bank Supervisors (CSBS). I appreciate the opportunity to testify on behalf of CSBS today on the subject of regulatory burden relief, and specifically H.R. 962.

As you know, CSBS is the professional organization of state officials that charter, examine, regulate, and supervise the activities of the over 8,800 state banks in this country. These banks hold over $1.5 trillion in assets and maintain an aggregate capital ratio of 7.9 percent.

Federal oversight of these institutions is provided by the Federal Deposit Insurance Corporation (FDIC) for nonmember banks and by the Federal Reserve System (Fed) for member banks. State bank supervisors across the country have developed close working relationships with the FDIC and the Fed to supervise state banks in what has proven to be an effective and efficient manner. The combined efforts of the state supervisors and our federal counterparts have resulted in banks that are more profitable, more highly capitalized, and above all, safer.

Regulatory Burden

Through your leadership, Mr. Chairman, and that of the original sponsors of H.R. 962, fellow Nebraskan Congressman Bereuter and Congressman Bacchus, you have begun the difficult task of addressing the excessive regulatory burdens imposed on the banking industry. Previous testimony has given detailed descriptions of the various provisions of the bill. Rather than review the specifics of that legislation, I will address CSBS's general view of regulatory burden and discuss some recent state efforts to reduce its impact on the banks we regulate.

At its most basic, state regulation of banking is guided by three important interrelated concepts. First, the institutions must operate in a safe and sound manner. Second, credit and payment services must be available to sustain communities and fuel economic growth. Third, consumers must be treated fairly.

The goal of state regulation is to strike a balance between these three non-conflicting principles. While innovations in the industry enhance all three, over-emphasizing any single concept works to the detriment of the other two. It is this perspective that we, as state regulators, hope to bring to the current discussions of regulatory burden.

A review of the federal banking legislation for the past five years shows that the unquestionable focus has been safety and soundness, and consumer protection. Recent attention to the credit

crunch has redirected the debate to the provision of credit and payment services. The question before this committee, and of concern to all of us involved in bank regulation, is whether certain regulations and requirements can be reduced or removed to increase the flow of credit while maintaining the safety of the banking industry and the protection of the consumer.

There is no simple answer to this question. As the hearings before this Subcommittee have shown, there are strongly held views on all sides. These are supported by reasonable and substantial arguments. We must forge ahead, however, because the current level of regulatory burden is increasingly influencing the long term soundness of the banking industry.

Testimony already received by this committee describes in detail the repercussions of current regulatory requirements on all institutions. The effects are particularly harsh on our smaller banks. These institutions are the ones which are the very life's blood of small town America.

The average asset size of the two hundred and fifty seven Nebraska state-chartered banks is less than $50 million. Across the United States, almost 2,000 banks have fewer than 10 full and part-time employees. An additional 3,900 banks have between 10 and 25 full and part-time employees. These two categories of banks make up 49 percent of the banking industry in this country.

As regulatory requirements increase, the vast majority of these institutions are simply not able to add the additional personnel necessary to keep track of compliance. That means that either the chief executive must allocate more time to that area, or other personnel must be reassigned.

We state regulators can all point to examples where a smaller institution has been forced to replace a loan officer with a compliance officer. Given the current regulatory environment, this is often the only choice for bank management. It has serious long term consequences, however, for both the bank and the area it serves.

The bank loses some ability to generate new business and to retain current business in the face of strong competition from other financial services providers who are not saddled with the same regulatory requirements. The bank's community loses some of the valuable financial expertise available to new businesses and small growing businesses from commercial loan officers. The overall result is slower economic growth and a decline in the creation of new jobs.

Of great concern, also, is the real possibility that this glut of regulations may adversely affect a bank's safety and soundness. As we all know, profitability is one way to measure the health of

an institution. It's clear that over-emphasis on compliance as described above will reduce profitability. Additionally, overregulation may serve to reduce the quality of loans made by the bank. We must remember that banks are a business, and need to be allowed to operate as such. Banking in general, and commercial lending in particular, are not "paint by numbers" undertakings. Just because all of the paperwork is correct and placed in the file in the proper order, the loan is not necessarily any good. One other critical factor comes into play: judgement.

The more we as regulators stress stringent compliance practices with specific requirements, the more likely we are to micro-manage some of our institutions into an early grave. In short, we have stopped being part of the solution and are finding ourselves to be part of the problem.

The banks are not alone in shifting their emphasis to compliance. Several of the federal regulators have also announced substantial increases in compliance staffs, including the reallocation of examiners from safety and soundness to compliance review. These recent events, coupled with the sometimes severe penalties associated with failure to comply, makes bankers' apparent obsession with compliance understandable. The question for bank regulators and for the members of this committee is whether this is appropriate.

<u>State Efforts to Reduce Regulatory Burden</u>

The state bank regulators have a long history of working with the FDIC and the Fed in the supervision of state banks. State regulators have also coordinated regulatory efforts among themselves and exchanged information and ideas on the improvement of the state banking system and state regulation, through CSBS. Recent changes in the banking industry and the requirement in the Federal Depository Insurance Corporation Improvement Act of 1991 (FDICIA) for annual on-site examinations of all banks have made these efforts at cooperation more important to both the regulators and the banks.

FDICIA required an annual examination for all banks. Well-managed banks of less than $100 million in assets were placed on an 18 month schedule. The FDIC and the Fed may accept state examinations on an alternating period basis and are encouraged to coordinate efforts with state regulators. In response to this legislation and in light of past efforts, CSBS entered into separate agreements with the FDIC and the Fed to promote a system of coordinated examinations of state banks.

The general points of the agreements with both agencies call for alternating state and federal examinations of healthy banks, generally CAMEL 1 or 2 rated banks. Banks with lower CAMEL ratings (3, 4, or 5) may be examined independently by the state and the

federal regulator as each deems necessary. Both the federal regulator and the state will coordinate on lower CAMEL rated banks to reduce redundancy and optimize the examination effectiveness and usefulness to both regulators. Alternating examinations are permitted for CAMEL 3 institutions if the federal agency and the state agree that the condition of the bank is stable and improving and the bank meets a variety of other criteria.

The agreement incorporated two additional noteworthy concepts. First, one factor in determining the acceptance of alternate examinations for CAMEL 3 banks is whether the state banking department is CSBS-accredited. CSBS Accreditation is an extensive review of the quality and professionalism of a state banking department. Each accredited state is reviewed annually and must undergo reaccreditation every five years. Twenty-eight states are currently accredited; my own department received this recognition earlier this year. These states regulate more than 75 percent of all assets in state-chartered banks.

The second concept included in the agreements is the allowance for concurrent and joint examinations in addition to alternating examinations. A joint examination involves an examination team made up of members from both the state and the federal agencies that produces a single examination report. A concurrent examination involves both agencies sending in teams of examiners simultaneously. Each agency produces a separate report. Each of these types of examinations is used to address specific concerns or local needs.

The advantage of these agreements is twofold. They minimize the time a bank is under examination and maximize the resources available to state and federal regulators. Each state signs an agreement with its respective Federal Reserve Bank and FDIC region. These individual agreements are modeled after the general agreement between CSBS and the federal regulators, but allow for flexibility to address local needs and conditions. At this time, 38 states have signed agreements with the FDIC and 14 with the Fed. Many other agreements are currently under discussion.

Interstate banking created a new challenge for bank regulators. Today, bank holding companies operate banks on a large scale in several states. This requires greater cooperation among the states and among federal regulators. In order to assess the overall health of an institution, each regulator needs information on the affiliates' operations in other states. The states sign agreements to share confidential supervisory information. These agreements have augmented those already existing between the states and the federal regulators.

Multistate bank holding companies also present the need for greater scheduling coordination among more agencies. In order to get an accurate picture of the health of the entire institution,

all of the affiliates and the parent holding company need to be examined within the same quarter. As nationwide banking takes hold, scheduling becomes more important. We are able to use the experience gained through supervising regional holding companies. Now in addition to several states, we often have several Federal Reserve Banks, FDIC and Office of the Comptroller of the Currency regional offices involved. This coordinated effort allows for a snapshot of the health of the institution while taking full advantage of the local knowledge and expertise of the various regulatory agencies.

Our experience with multistate bank holding companies is providing benefits in another area. We now have several holding companies whose subsidiary banks are primarily state-chartered. By coordinating our efforts among the states and the federal regulators, we can substantially reduce the institution's time and expense while enhancing the quality of an examination. We have also found virtually all states and federal regulators to be flexible in their own requirements to make these advances possible.

One example of these advances is a common entry letter. The entry letter to an institution lists the information needed by the examiners. This information varies from time to time depending of the areas of interest to the examining agency and the results of off-site monitoring. We found that there is a core of information that all entry letters require, but slight variations in the requests often require a bank to produce separate data for each examining agency. With a common core, the bank could produce one data report that met the general needs of the examining agencies. Each agency, both state and federal, could request additional information to meet their individual needs. This lowered banks' examination costs while providing full and complete information to the examiners.

Additional Regulatory Concerns

There are three other topics I would like to address briefly before closing. The first is the issue of the FDIC's back-up authority over national banks and federal savings associations. In FDICIA, the FDIC was given back-up examination and enforcement authority over national banks. This authority is similar to that granted the FDIC over federal savings associations in the 1989 Financial Institutions Reform, Recovery and Enforcement Act (FIRREA). It gives the FDIC the authority to examine any FDIC-insured institution if it believes that it is necessary. The FDIC can also issue enforcement actions if the primary regulator fails to act.

This authority is critical to the continued solvency of the deposit insurance funds. The FDIC, as deposit insurer, should have the ability to examine independently any institution it insures without undue restriction. Some have suggested in testimony before

this committee that the FDIC back-up authority be reduced. There have also been some discussions of severely limiting the FDIC's discretion administratively. We believe that these restrictions are counter to the intent of FDICIA and FIRREA and are counter to the best interest of the taxpayer guarantee of the deposit insurance funds. We strongly urge you to oppose any reduction in back-up authority of the FDIC.

The second issue is the importance of flexibility in the supervision of the banking industry. Whether it is regulatory innovations or new products and services, both the regulators and the banks must be allowed the flexibility to meet changing market conditions. FDICIA placed a straitjacket on both federal and state regulators by removing much of the discretion and judgement needed to supervise a dynamic and changing banking industry.

To the extent that we the regulators are limited, so too are the banks restricted in addressing new competitive pressures and market needs. As a result, the market share of commercial banks has declined from over 40% in the mid-70s to 23% today. Most of the market share has gone to less-regulated nonbank banks. Thus, the new regulations and compliance procedures often become a road block and not a catalyst to new growth. There is no doubt that our bankers today have to spend more and more time on new regulations and compliance, time which could be better spent serving customers and fulfilling the needs of small business. We ask you to consider these issues as you address this and other legislation.

At their recent meeting, the nation's governors passed a resolution proposed by Nebraska Governor E. Benjamin Nelson expressing their concern over the effect of excessive bank regulation on credit availability. In their resolution, the governors called on the state regulators to make recommendations for regulatory relief. We at CSBS are currently working on these recommendations and will provide them to this committee very soon.

In closing, let me thank all of the members of this committee, who have already struck a significant blow against costly regulatory burden. Earlier this year, you defeated the state examination fee proposal contained in the budget resolution. Your action saved the banking industry over $1.3 billion in additional, unnecessary costs, keeping these funds available for lending to support economic growth. In Nebraska alone, where the cost of regulation to state banks would have tripled, it saved over $12 million. We appreciate your efforts to defeat the state examination fees and ask for your continued opposition to its imposition.

I will be happy to answer any questions. Thank you.

ORAL STATEMENT OF JIM HANSEN

Chairman Neal, Mr. McCollum, and Members of the Committee, my name is Jim Hansen. I am the Director of Banking and Finance for the State of Nebraska and Vice Chairman of the Conference of State Bank Supervisors, CSBS. I appreciate the opportunity to testify on behalf of CSBS today on the subject of regulatory burden relief, and specifically H.R. 962.

Through your leadership, Mr. Chairman, and that of the original sponsors of H.R. 962, fellow Nebraskan Congressman Bereuter and Congressman Bacchus, you have begun the difficult task of addressing the excessive regulatory burdens imposed on the banking industry. Previous testimony has given detailed

descriptions of the various provisions of the bill. Rather than review the specifics of that legislation, I will address CSBS's general view of regulatory burden.

Basically, state regulation of banking is guided by three important interrelated concepts. First, the institutions must operate in a safe and sound manner. Second, credit and payment services must be available to sustain communities and fuel economic growth. Third, consumers must be treated fairly.

The goal of state regulation is to strike a balance between these three non-conflicting principles. While innovations in the industry enhance all three, over-

emphasizing any single concept works to the detriment of the other two.

A review of the federal banking legislation for the past five years shows that the unquestionable focus has been safety and soundness, and consumer protection. The question before this committee, and of concern to all of us involved in bank regulation, is whether certain regulations and requirements can be reduced or removed to increase the flow of credit while maintaining the safety of the banking industry and the protection of the consumer.

There is no simple answer to this question. We must forge ahead, however, because the current level

of regulatory burden is negatively impacting the long term soundness of the banking industry.

The entanglement of the regulatory requirements are at least partially to blame for the inability of banks to respond to the competitive environment of the financial industry today. As a result, the market share of commercial banks has declined from over 40% in the mid-70s to approximately 23% today. Most of the lost market share has gone to less-regulated competitors, such as securities firms and mutual funds.

New regulations and compliance procedures often are a road block to new growth. Testimony already received by this committee describes in detail the repercussions of current regulatory requirements on all

banks. The effects are particularly harsh on our smaller banks. These institutions are the ones which are the very life's blood of small town America.

Across the United States, almost 2,000 banks have fewer than 10 employees. An additional 3,900 banks have between 10 and 25 employees. These two categories of banks make up 49 percent of the banking industry in this country. In Nebraska, the average asset size of the 257 state-chartered banks we regulate is less than 50 million dollars.

As regulatory requirements increase, the vast majority of these institutions are simply not able to add the additional personnel necessary to keep track of

compliance. That means that either the chief executive must allocate more time to that area, or other personnel must be reassigned.

Of great concern, also, is the real possibility that this glut of regulations may adversely affect a bank's safety and soundness. As we all know, profitability is one way to measure the health of an institution. The burden of regulation is reducing profitability. Additionally, overregulation may serve to reduce the quality of loans made by the bank. We must remember that banks are a business, and need to be allowed to operate as such. Banking in general, and commercial lending in particular, are not "paint by numbers" undertakings. Just because all of the paperwork is

correct and placed in the file in the proper order, the loan is not necessarily any good. One other critical factor comes into play: judgement.

Banks are not alone in shifting their emphasis to compliance. Several of the federal regulators have also announced substantial increases in compliance staffs, including the reallocation of examiners from safety and soundness to compliance review. These recent events, coupled with the sometimes severe penalties associated with failure to comply, makes bankers' apparent obsession with compliance understandable. The question for bank regulators and for the members of this committee is whether this is appropriate.

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There are two other topics I would like to address briefly before closing. The first is the issue of the FDIC's back-up authority over national banks and federal savings associations This authority is critical to the continued solvency of the deposit insurance funds. The FDIC, as deposit insurer, should have the ability to independently examine any institution it insures. Some have suggested in testimony before this committee that the FDIC back-up authority be reduced. Earlier this week the FDIC Board voted to restrict its examination of federally-chartered institutions. We believe that these restrictions are counter to Congressional intent and counter to the best interest of the taxpayer guarantee of the deposit insurance funds. We strongly urge you to oppose any reduction in back-

up authority of the FDIC.

The second issue is the importance of flexibility in the supervision of the banking industry. Whether it is regulatory innovations or new products and services, both the regulators and the banks must be allowed the flexibility and creativity to meet changing market conditions. FDICIA placed a straitjacket on both federal and state regulators by removing much of the discretion and judgement needed to supervise a dynamic and changing banking industry. We ask you to consider these issues as you address this and other legislation.

In closing, let me thank all of the members of this

committee, who have already struck a significant blow against costly regulatory burden. Earlier this year, you defeated the state examination fee proposal contained in the budget resolution. Your action saved the banking industry over 1.3 billion dollars in additional, unnecessary costs, keeping these funds available for lending to support economic growth. In Nebraska alone, where the cost of regulation to state banks would have tripled, it saved over $12 million dollars. We appreciate your efforts to defeat the state examination fees and ask for your continued opposition to its imposition.

I will be happy to answer any questions. Thank you.

United States General Accounting Office

GAO

Testimony

Before the Subcommittee on Financial Institutions Supervision, Regulation and Deposit Insurance, Committee on Banking, Finance and Urban Affairs House of Representatives

For Release on Delivery
Expected at
9:30 a.m.
Thursday,
September 23, 1993

BANK AND THRIFT REGULATION

FDICIA Safety and Soundness Reforms Need to Be Maintained

Statement of Donald H. Chapin
Assistant Comptroller General
Accounting and Information Management Division

GAO/T-AIMD-93-5

Mr. Chairman and Members of the Subcommittee:

We are pleased to have the opportunity to discuss H.R. 962, the Economic Growth and Financial Institutions Regulatory Paperwork Reduction Act of 1993. You asked for our comments on the effect this bill would have on credit availability and the safety and soundness of the industry. H.R. 962 contains many different provisions that are intended to reduce the burden of regulation on safe, sound, and properly managed financial institutions. While we are not in a position to comment on most of these provisions based on work we have performed, I want to emphasize GAO's support for efforts to reduce regulatory burden that does not compromise safety and soundness or other public interests. Earlier this month we issued a report that recommended ways to reduce the regulatory burden on small business lending,[1] and we have other work underway that I will discuss later.

We are concerned about several provisions of H.R. 962 that would weaken some of the safety and soundness reforms that were enacted by the Congress less than 2 years ago, many of which are still being implemented. These provisions run the risk of undoing much of the progress that has been made in reforming safety and soundness regulation without any assurance that they would spur much bank lending. Rolling back these reforms would place taxpayers needlessly at risk and could undermine other legislative

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[1]Bank Regulation: Regulatory Impediments to Small Business Lending Should Be Removed (GAO/GGD-93-121, September 7, 1993).

efforts, such as interstate branching, to modernize the banking industry.

We believe that there are opportunities to reduce the regulatory burden that should be vigorously pursued by both the administration and the Congress. But in proceeding, it is important to consider all relevant benefits of regulation, as well as costs, together with longer term goals for the modernization of the banking industry.

My testimony is divided into two parts. First, based on work completed and in progress, I would like to provide some general comments on reducing regulatory burden, including a discussion of our small business lending report. Next, I will explain our concerns about the implications of the changes to safety and soundness provisions proposed by H.R. 962.

GAO WORK ON REDUCING REGULATORY BURDEN

The many provisions of H.R. 962 illustrate the wide range of topics that can be potentially addressed under regulatory burden. As the Subcommittee is aware, we have a study underway that is intended to develop greater understanding of burden issues. We are analyzing studies by industry groups and the banking agencies to understand the methodology they have used in addressing burden and to see

whether there are burden issues that can be clearly identified as high priorities. We anticipate that our report will be available by the end of the year. In another study, we are looking much more in depth at the Community Reinvestment Act. Through this study, we intend to review the industry's experience with the act and related fair lending laws from the perspective of bankers, regulators, and community groups. We anticipate that this study, which will focus on about 50 to 60 banks, will be finished in the spring.

Our work to date has given us an appreciation of the complexities of the regulatory burden issues. It is hard to find reliable data. Furthermore, while the cost of bank regulation is a vital issue for the industry and for the financial sector of the economy, it is also necessary to consider the benefits associated with regulation. Taken as a whole, the regulatory structure applicable to depository institutions is designed to benefit the public by providing industry stability, protection of depositor funds, and the availability of banking services. The system has also provided many benefits to the institutions themselves. These benefits include the right to accept insured deposits and access to the Federal Reserve's discount window. The markets have also allowed banks to operate with lower amounts of equity capital than markets may otherwise require without federal deposit insurance.

In view of this, the task of reducing the burden of regulation requires a careful assessment of the costs and benefits of proposed

changes. In doing this, it is also important to distinguish between changes that may require legislation and those which can be dealt with by changes in agency regulations or supervision.

Small Business Lending

As I mentioned, earlier this month we issued a report on small business lending. We were asked to conduct this study to gain insights into ways safety and soundness regulation or supervision may be inhibiting the ability of sound banks to make traditional small business loans (loans to established businesses for such things as working capital and equipment) that would otherwise be justified by market conditions.

In part, this assignment involved unstructured interviews with officials in 38 banks of different sizes in 8 states as well as discussions with regulators. Our sample of banks was not intended to be a random sample and therefore the views expressed are not necessarily representative of the industry as a whole. We were, however, struck by the consistency with which bankers told us that compared to several years ago, they were seeking assurance that loans could be repaid from the businesses' cash flows. They attributed this shift toward tighter, more traditional credit standards, primarily to a response to the extraordinary loan losses incurred by the industry in the late 1980s and early 1990s, and

also to current uncertain economic conditions, particularly in some regions of the country.

However, there were two areas--real estate appraisals and bank examinations--where many felt that regulations were placing an excessive burden on the small business lending activities of sound banks. In looking more closely at these two areas, we found that there are actions that federal banking agencies can take to reduce regulatory impediments to small business lending without compromising essential safety and soundness standards. These actions do not require legislation and would make it clear that sound banks have flexibility in applying good business practices to their small business lending programs.

Turning first to appraisals--because inadequate or overstated appraisals contributed to costly thrift and bank failures during the 1980s--Congress directed the banking agencies in 1989 to strengthen the requirements for estimating the value of real estate that is to be pledged as collateral for a loan. While there is no question that action to correct abuses was needed, a problem for traditional small business lending was created by the broad scope of the implementing regulations and agency guidance. The agencies in essence required banks to obtain formal appraisals of real estate given as collateral for a traditional small business loan, even though banks expected the loan to be paid from the cash flow of the business. Bankers with whom we spoke told us that these

appraisals would generally cost the borrower about $3,000 or more and could delay processing a loan. The appraisal issue is important because in today's credit environment small companies are frequently required to provide collateral for loans. For example, one larger bank we contacted estimated that real estate is used to collaterize over 60 percent of its small business loans.

We concluded that real estate appraisal requirements can be safely modified when applied to collateral taken as supplementary support for traditional small business loans. Therefore, we agree with those aspects of the pending rule changes that have been recently proposed by the banking regulators to exampt such loans from a mandatory appraisal requirement.

We also concluded that the banking agencies needed to clarify the guidance given to banks about how to evaluate real estate collateral when an appraisal is not required. Currently, this guidance is not consistent and is subject to varying interpretation by banks. We recommend that the agencies make it clear that bankers in sound institutions can use their judgment in determining the most cost-effective way to evaluate the collateral for small business loans that are immaterial to the condition of a bank.

In the supervision area, in an effort to spur bank lending, the agencies have undertaken an interagency policy initiative to allow banks with adequate capital and satisfactory management to place

some loans in a "basket" with minimum documentation requirements and examiner attention. Many of the bankers with whom we spoke said this regulatory initiative will likely have a limited impact on small business lending because, as indicated earlier, banks have voluntarily increased their documentation and underwriting standards. Moreover, banks using the minimum documentation requirements will have to track those loans separately.

Allowing sound institutions greater flexibility in the administration of their small business loan program makes sense and is consistent with the approach to regulation contained in the FDIC Improvement Act of 1991 (FDICIA), which underscores the importance of capital and management and makes distinctions among institutions based on their soundness. We also believe that an effective way for the agencies to ensure that the examination process does not inhibit the small business lending activities of sound institutions is to focus their examinations on the institutions' systems of internal controls. If tests of controls show that a bank is adhering to good underwriting and credit administration policies, examiners would not have much reason to challenge management's judgments regarding individual small business loans.

In the near term, the changes we recommended with regard to appraisals and supervision are not likely to make a big difference in the volume of lending because of the importance of other factors, such as demand for loans. However, these changes are

nonetheless important because they would help soundly managed institutions to respond more confidently to an increase in loan demand. Building up a greater degree of trust between the industry and the regulators, based on a common understanding of good business practices, can only be beneficial to the economy.

Simplifying the
Supervisory Process

In February 1993, we testified on the results of our review of the bank and thrift regulators' safety and soundness examinations.[2] We identified inconsistencies and overlap in the four regulators' examination policies and practices. These inconsistencies included differences in examination scope, frequency, documentation, and assessment of critical areas, such as loan loss reserves. Such differences could result in disparate conclusions regarding the safety and soundness of an institution, depending on which regulator does the assessment.

Although we did not study the efficiency and effectiveness of the regulatory structure as a whole, we believe the examination overlap and inconsistencies we found are symptomatic of the difficulty of efficiently and effectively regulating the banking and thrift industries with four separate federal regulators. The current

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[2]Bank and Thrift Regulation: Improvements Needed in Examination Quality and Regulatory Structure (GAO/T-AFMD-93-2, February 16, 1993).

regulatory structure has evolved over decades of legislative efforts to address specific problems, resulting in a fragmented system that may no longer be capable of handling the complexities of today's banking and thrift industries. We believe that the system's weaknesses result in the potential for inequitable regulation of banks and thrifts and may place an unnecessary burden on the industry. We believe the inefficiencies in the regulatory examination process also extend to the overlap between the work conducted by the examiners in reviewing loans and related internal controls and the work of the banks' external auditors. Although legislation is needed to restructure the regulatory agencies, FDICIA already provides the basis for the regulators and auditors to better coordinate their work.

SAFEGUARDS TO PROTECT THE BANK AND THRIFT INSURANCE FUNDS SHOULD NOT BE WEAKENED

While we support efforts to reduce regulatory burden, we are concerned about proposals that would eliminate or reduce the effectiveness of some of FDICIA's safety and soundness reforms. From 1980 through 1992, approximately 2,700 banks and thrifts failed, costing the insurance funds and taxpayers roughly $200 billion. FDICIA's reforms are essential for protecting healthy banks and the taxpayers from excessive deposit insurance costs.

The key FDICIA safety and soundness provisions are (1) requirements for prompt corrective action for institutions failing to meet specified capital and safety and soundness standards, (2) management and auditing reforms for institutions with assets of $150 million or more (raised to $500 million by FDIC regulations) that highlight private sector responsibility for protecting taxpayers from losses, (3) accounting reforms to provide accurate information to management, regulators, and the public, (4) annual, on-site examinations for most institutions to detect problems on a more timely basis, and (5) changes in the way institutions are closed so that uninsured depositors and general creditors will be more likely to share in the losses if an institution fails.

H.R. 962 proposes eliminating or altering several of FDICIA's safety and soundness reforms concerning prompt regulatory action supervisory and accounting requirements. The stated purpose of H.R. 962 is "to increase the amount of credit available to fuel local, regional, and national economic growth by reducing the regulatory burden imposed upon safe, sound, and properly managed financial institutions." We believe the proposals to change the safety and soundness requirements, although well intended, are misguided and may very well have the effect of removing early warning signals of safety and soundness problems and therefore eliminating the opportunity for both bank management and regulators to correct problems before they overwhelm the institution and result in losses to the deposit insurance funds.

The prompt corrective action, supervisory, and accounting and auditing provisions of FDICIA are critically linked to protect the insurance funds. In other words, the examiner visits the institution once a year to observe its functioning first-hand, management is required to protect the insurance funds through effective corporate governance, and guidance is provided to the regulators to ensure that banks and thrifts maintain the minimum capital levels and safety and soundness standards to guard against losses to the insurance funds. In addition, the accounting provisions are fundamental to ensure financial reports that accurately reflect the financial condition of the institution and to facilitate effective supervision and, if necessary, action to resolve troubled institutions at the least cost to the insurance funds.

We have issued reports and testified a number of times concerning why the reforms I just discussed are so important.[3] We have

[3]Bank Failures: Independent Audits Needed to Strengthen Internal Control and Bank Management (GAO/AFMD-89-25, May 31, 1989).

Thrift Failures: Costly Failures Resulted from Regulatory Violations and Unsafe Practices (GAO/AFMD-89-62, June 16, 1989).

Financial Condition of the Federal Deposit Insurance Corporation's Bank Insurance Fund (GAO/T-AFMD-89-15, September 19, 1989).

Prevention, Detection, and Reporting of Financial Irregularities (GAO/T-AFMD-90-27, August 2, 1990).

Bank Insurance Fund: Additional Reserves and Reforms Needed to Strengthen the Fund (GAO/AFMD-90-100, September 11, 1990).

Additional Reserves and Reforms Are Needed to Strengthen the Bank Insurance Fund (GAO/T-AFMD-90-28, September 11, 1990), letter to

analyzed the bank and thrift failures and the effectiveness of enforcement actions taken by the regulators. The consistent finding was that serious managerial and internal control weaknesses contributed significantly to the failures and that enforcement actions were not forceful or timely enough to correct the problems identified by the examiners. Also, flexible accounting rules allowed institutions to hide their losses.

In our review of audit committees[4] of banks with $10 billion or more in assets, many audit committee chairmen told us their members lacked independence, the expertise related to their

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the Chairmen, Senate Committee on Banking, Housing and Urban Affairs (B-114831, September 13, 1990), and letter to the Chairman and Ranking Minority Member, House Committee on Banking, Finance and Urban Affairs (B-114831, September 21, 1990.

Deposit Insurance: A Strategy for Reform (GAO/GGD-91-26, March 4, 1991).

Deposit Insurance: A Strategy for Reform (GAO/T-GGD-91-12, March 7, 1991).

Bank Supervision: Prompt and Forceful Regulatory Actions Needed (GAO/T-GGD-91-15, March 14, 1991).

Bank Supervision: Prompt and Forceful Regulatory Actions Needed (GAO/GGD-91-69, April 15, 1991).

Failed Banks: Accounting and Auditing Reforms Urgently Needed (GAO/AFMD-91-43, April 15, 1991).

Bank Supervision: OCC's Supervision of the Bank of New England Was Not Timely or Forceful (GAO/GGD-91-128, September 16, 1991).

OCC Supervision of the Bank of New England (GAO/T-GGD-91-66, September 19, 1991).

[4]Audit Committees: Legislation Needed to Strengthen Bank Oversight (GAO/AFMD-92-19, October 21, 1991).

responsibilities as audit committee members, and adequate information on internal controls and compliance with laws and regulations in key areas of bank operations. Clearly this is an unacceptable situation.

Audit committees are intended to play a very important role in the corporate governance of banks. Their responsibilities should include monitoring banks' internal controls and ensuring that management is not overriding internal controls, supervising the activities of internal and external auditors, and reviewing financial statements and important accounting policies. Audit committees need to be made up of independent outside directors to enable an impartial review of managemsnt's conduct of bank business.

FDIC Issued Limited Regulations
to Implement Section 112 of FDICIA

Section 112 of the act pertains to management and auditor reporting on internal controls and compliance with safety and soundness laws and regulations designated by FDIC, and to independent audit committee requiremsnts. FDIC elected to issue limited regulations to implemant section 112 and also to provide minimal guidelines. In FDIC's discussion of the final rule issued June 2, 1993, FDIC stated that its approach was consistent with the letter and spirit of the law and with comments received that the final rule "not

impose unnecessary regulatory burdens, provide appropriate flexibility, and be reasonably cost-effective."

In this case, we believe that FDIC has allowed institutions too much flexibility with respect to the section 112 requirements. We advised the FDIC Board of Directors on May 10, 1993, that such limited regulations and guidance would result in a serious weakening of the act's reforms, which were intended to prevent a recurrence of the breakdowns in internal controls and flawed systems of corporate governance that contributed to the savings and loan crisis and bank failures. H.R. 962 was introduced on February 18, 1993, before the final FDIC regulations were issued in May 1993. Given FDIC's actions, we believe it would be a serious mistake to further weaken the corporate governance reforms as proposed by H.R. 962.

Regulators Have Written Proposed General Standards to Implement Section 132 of FDICIA

Section 132 of FDICIA adds a noncapital component to the prompt corrective action provisions. Among other things, it requires regulators to establish various operational and managerial standards in the areas of internal controls, information systems, internal audit systems, loan documentation, credit underwriting,

interest rate exposure, and asset growth. These provisions are to become effective no later than December 1, 1993.

We believe Section 132 is a crucial component of prompt corrective action. Because falling capital levels are a lagging indicator of problems in a bank or thrift, this section provides regulators a basis for acting earlier to correct unsafe and unsound practices. These provisions, therefore, need to be enforced at all institutions and we oppose H.R. 962's proposals to selectively implement these requirements.

Section 132 has been widely misunderstood to call for highly detailed and restrictive rules for bank behavior. I see no reason why regulations have to lead to such a result, nor does FDICIA require it. On the contrary, actions by the regulators to establish the standards are in the opposite direction. In July 1992, the regulators issued an advance notice of proposed rulemaking to obtain public comments on all aspects of the safety and soundness standards. The majority of comments received were from insured depository institutions and holding companies. Those who commented recommended that the regulators adopt general rather than specific standards in order to avoid regulatory micromanagement of the banking and thrift industries.

Based on these comments, the regulators are now preparing proposed regulations for public comment. A draft of the proposed rulemaking

has been approved by FDIC and the Federal Reserve Board and is currently being reviewed by Treasury. The draft proposed regulations state that the "proposed standards are specific enough to identify emerging safety and soundness problems and require submission of a compliance plan before those problems become serious; however, the standards do not specify each operational and managerial procedure an institution must have in place." For example, the

> "proposed regulations do not specify in detail what loan documentation must contain. Instead, they specify what loan documentation must enable an institution to do. Thus, documentation practices at an institution will not be evaluated against a checklist of requirements but instead will be evaluated based on whether they: (1) enable the institution to make an informed lending decision and to assess risk as necessary on an ongoing basis; (2) identify the purpose of the loan and the source of repayment, and assess the ability of the borrower to repay the indebtedness in a timely manner; (3) ensure that any claim against a borrower is legally enforceable; (4) demonstrate appropriate administration and monitoring of a loan; and (5) take account of the size and complexity of a loan. The agencies believe that the proposed regulation provides a standard against which compliance can be measured, while at the same time allowing for differing approaches to loan documentation."

We agree with the regulators that "under the proposed regulations, well-managed institutions generally should not find it necessary to amend their operations in order to comply with the operational and managerial standards."

Rules for Fair Market Value Disclosures Required by Section 121 of FDICIA Not Yet Completed

The accounting reforms required by Section 121 of FDICIA include reporting by banks and thrifts of the estimated fair market value of their assets and liabilities to the extent feasible and practicable. The regulators are currently evaluating comments they received on the feasibility of such reporting. H.R. 962 would repeal the FDICIA market value disclosure requirements.

We believe disclosure of the fair value of assets and liabilities is information that regulators need to fully understand the financial condition and activities of banks and thrifts. Generally accepted accounting principles are largely based on reporting that uses historical costs, which may differ significantly from fair values. Also, institutions may have activities off the balance sheet that equal or exceed their assets and liabilities reported on the balance sheet. The failed Bank of New England is an example of an institution that reported about $30 billion in assets on its balance sheet and had about an equal amount of off-balance

activities that exposed the bank to potential losses. In that respect, the widespread use of derivative products, both by large banks, who are dealers and end users of products, and smaller institutions, who are generally end users, is another important reason for disclosure of fair market values. While derivative products, properly used, are valuable tools for hedging interest rate risks, they can be extremely complex and can involve substantial risk of loss.

Currently, accounting rules require disclosure of information about financial instruments with off-balance sheet risk of loss. Also, entities are required to disclose the fair value of financial instruments, both assets and liabilities recognized on the balance sheet and those not recognized, for which it is practicable to estimate fair value.[5] If estimating fair value is not practicable, entities are required to disclose information pertinent to estimating fair values of financial instruments and why it is not practicable to estimate fair value. The FDICIA requirement parallels current accounting rules, although it extends fair value disclosures to nonfinancial assets and liabilities. Although the regulators are correct in obtaining public comments regarding the feasibility of enhanced disclosure requirements, we believe that any exceptions allowed by the regulators in the final regulations should be clearly justified. In addition, we believe

[5]For entities with less than $150 million in total assets, these asset/liability disclosure requirements are effective for fiscal years ending after December 15, 1995.

that consistent with current accounting rules, the final regulations should require that reports submitted by institutions to the regulators that do not disclose fair market values for reasons of practicality should explain why it is not feasible to do so.

Improved Industry Performance Does Not Mean Essential Safeguards Should Be Removed

The performance of the banking and thrift industries has rapidly improved by any number of indicators--be it net income, return on assets, or capital levels. The rapid turnaround of the banking industry in particular demonstrates the volatility of the business of banking and its effect on the Bank Insurance Fund. It took just 4 years to deplete the Fund's 1987 net worth of $18.3 billion. In about 18 months, the Fund's balance has improved from a $7 billion deficit at December 31, 1991, to an unaudited balance of about $6 billion at June 30, 1993. We agree with the statement made by the Acting FDIC Chairman when releasing the June 30 numbers that caution is needed. The Fund's reserve levels are 35 cents for every $100 of insured deposits, well below the reserve of $1.25 designated by the Federal Deposit Insurance Act. The number of problem banks, although decreasing, standa at 640 with assets of $363 billion.

The improved condition of the Fund is attributable to increased insurance assessment income as well as substantial declines in actual and estimated losses from bank failures. Extraordinary interest rate spreads in 1992, continuing into 1993, rescued a number of failing banks and are largely responsible for the turnaround in the condition of the industry. The safety and soundness reforms of FDICIA, particularly the prompt corrective action requirements, have provided incentives to build capital and maintain financial stability as industry conditions improved.

It is important to understand that the prompt corrective action, supervisory, and accounting and auditing requirements collectively serve to provide an early warning of conditions that may need both bank management and regulator attention before they turn into serious problems. Accepting deposits and investing them in loans makes banking an inherently risky business, as demonstrated by the banks' experience with transactions involving lesser developed countries, leveraged buyouts, and commercial real estate. Large banks are now using highly complex financial derivatives that can expose them to credit and market risks. Breakdowns in internal controls need to be identified before deterioration of asset values and losses occur and capital levels are eroded. FDICIA's intent should be viewed as providing all banks and thrifts with incentives to operate with sound controls, and well managed banks should have no trouble meeting such standards.

In summing up the importance of the safeguards provided by FDICIA, it is essential that we not lose sight of the market environment that makes the new reforms so essential. In today's competitive markets, banks and thrifts must be well capitalized and have good management controls to operate safely and to protect the insurance funds. The safety and soundness reforms proposed to be eliminated or altered by H.R. 962 may inadvertently cause banks and thrifts and their regulators to pay insufficient attention to the realities of sound banking in the current environment.

CONCLUSIONS

In conclusion, we want to encourage efforts to identify and reduce burden when there is a clear benefit to do so. At the same time, we believe the Congress, the administration, and the regulators should exercise great caution in considering short-term measures to encourage more liberal lending practices by insured institutions. Over time, a healthy banking industry is the best support for the economy, and it would not be prudent, in my opinion, to attempt to periodically weaken and tighten bank regulation in response to recession and inflation. Had the banking system not dissipated its capital in the 1980s by making so many bad loans, it would have been better able to handle some of the problems encountered as the economy slowed. As the FDICIA reforms take hold, we can be more confident of the regulators' ability to successfully supervise banks in today's compatitive market place and during times of

future economic distress. It also becomes more feasible for the Congress to consider ways of expanding the business opportunities for the industry without placing the deposit insurance system and the taxpayers at risk.

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GAO

United States
General Accounting Office
Washington, D.C. 20548

Accounting and Information
Management Division

October 27, 1993

The Honorable Stephen L. Neal
Chairman
The Honorable Bill McCollum
Ranking Minority Member
The Honorable Jim Bacchus
Member
Subcommittee on Financial Institutions
Supervision, Regulation and Deposit
Insurance
Committee on Banking, Finance and
Urban Affairs
House of Representatives

Enclosed are our answers to the questions you asked us to provide for the record regarding the hearing on H.R. 962, the Economic Growth and Financial Institutions Regulatory Paperwork Reduction Act of 1993, held on September 23, 1993. As was requested during the hearing, we are providing comments on each section o the bill where we have sufficient information to provide a response.

As stated in our testimony we are concerned about several provisions o H R 9 2 that would weaken some of the safety and soundness reforms that were enacted by the Congress less than 2 years ago, many of which are still being implemented. We oppose such changes as we believe they would place the insurance funds and taxpayers needlessly at risk However as stated in our comments there are a number of provisions in H R. 962 that we believe have potential for reducing regulatory burden Our existing work supports some of these provisions. We also have work underway that should be helpful in identifying other ways to reduce regulatory burden. In a number of other instances, we have not studied the issues involved.

If you would like to discuss our responses or need further assistance on these matters, please contact me or Robert W. Gramling, Director, Corporate Financial Audits at (202) 512-9406, or James L. Bothwell, Director, Financial Institutions and Markets Issues at (202) 512-8670.

Donald H. Chapin
Assistant Comptroller General

Enclosures

Questions from the Honorable Stephen L. Neal for Mr. Donald Chapin, Assistant Comptroller General, General Accounting Office

Question 1: The bank regulatory agencies have published for comment a proposal to raise the de minimis threshold for real estate appraisals from property valued at $100,000 to $250,000. Does GAO support that proposal?

Answer: Currently, we do not have a position on whether the de minimis threshold should be raised. We do, however have a study underway to assess the adequacy and quality of appraisals and evaluations for real estate below the de minimis threshold level This study, which is required by section 954 of the Housing and Community Development Act of 1992 and due in April 1994, may provide some insights on the benefits and risks involved in raising the de minimis level for commercial and residential properties

In our recent report on small business lending (Bank Regulation: Regulatory Impediments to Small Business Lending Should Be Removed, GAO/GGD-93-121, September 7, 1993), we supported eliminating the requirement for appraisals when real estate is used for collateral for ordinary small business loans (working capital, equipment purchases, etc.), provided that the real estate is not looked to as a primary source of repayment of the loans.

Question 2: Regulators require financial institutions to file statements of conditions commonly referred to as call reports, that are approximately 30 pages long. Please provide your analysis of whether all the information on the call report is essential to monitor the safety and soundness of financial institutions Please provide your specific recommendations of any information requested on call reports which could be eliminated without decreasing the safety and soundness of regulation

Answer: We have not studied the call report form to be able to reach an opinion as to whether all of the existing information is needed The call report is long, and we support efforts to simplify it. We have also urged the regulators to reduce the burden by developing arrangements for electronic filing. At the same time it is important to recognize the necessity of having timely, relevant information available to the regulators to be able to understand the risks in insured institutions. Developing adequate information in this way can help to reduce other, more time consuming and potentially burdensome supervisory activities.

Question 3: In your testimony, you pointed out that guidance to banks concerning evaluation of real estate collateral is inconsistent. Does that lack of consistency point to a large problem of having too many banking agencies and a need for a consolidation of the regulators?

Answer: The lack of consistency in evaluating real estate is an example of the difficulties of achieving uniform requirements with four regulators. Our review of bank and thrift regulatory examinations[1] disclosed significant inconsistencies among the regulators in their examination policies and practices. These inconsistencies included differences in examination scope, frequency, documentation, and assessment of critical areas, such as loan loss reserves. Such differences could result in disparate conclusions regarding the safety and soundness of an institution, depending on which regulator does the assessment

Although we did not study the efficiency and effectiveness of the regulatory structure as a whole we believe the examination problems and inconsistencies we found are symptomatic of the difficulty of efficiently and effectively regulating the banking and thrift industries with four separate federal regulators The current regulatory structure has evolved over decades of legislative efforts to address specific problems, resulting in a fragmented system that may not be the best approach for handling the complexities of today's banking and thrift industries.

[1] Bank and Thrift Regulation: Improvements Needed in Examination Quality and Regulatory Structure (GAO/AFMD-93-15, February 16, 1993), Bank Examination Quality: OCC Examinations Do Not Fully Assess Bank Safety and Soundness (GAO/AFMD-93-14, February 16, 1993), Bank Examination Quality: FRB Examinations and Inspections Do Not Fully Assess Bank Safety and Soundness (GAO/AFMD-93-13, February 16, 1993), Bank Examination Quality: FDIC Examinations Do Not Fully Assess Bank Safety and Soundness (GAO/AFMD-93-12, February 16, 1993), and Thrift Examination Quality: OTS Examinations Do Not Fully Assess Thrift Safety and Soundness (GAO/AFMD-93-11, February 16, 1993).

<u>Question 4</u>: Under the Consumer Credit Protection Act, the Federal Reserve is given the responsibility to adopt regulations for the various consumer laws. The other agencies have no regulatory authority, but simply enforce the Federal Reserve regulations. Should that model be adopted in other regulatory areas as well, so as to assure regulatory consistency?

<u>Answer</u>: Because there would be one ultimate decisionmaker, having a single rule making body would certainly address the coordination problems noted in response to the previous question. However, we are not in a position to say whether the rule making powers of the Federal Reserve Board should be expanded in an effort to simplify the rule making process.

So long as there are multiple regulatory agencies, problems in coordination will be encountered. We believe that if changes in rule making authority are contemplated, it would be preferable to consider them in the context of a more comprehensive restructuring of the banking regulatory structure.

<u>Question 5</u>: This year banks will file almost 10 million currency transaction reports (CTRs). How significant are these reports in deterring or detecting money laundering?

<u>Answer</u>: Federal and state law enforcement and regulatory agencies agree that the reports make a substantial contribution in deterring and detecting money laundering. The reports are valuable in several respects. First, it is generally recognized that improved compliance with the reporting requirements by banks has forced launderers to use much more difficult methods for placing large amounts of currency into the financial system. These methods include using currency exchanges, retail businesses, and physically smuggling the cash out of the country, all of which involve greater risk of detection. According to several Treasury studies and reviews by the Financial Crime Enforcement Network, the reports are also extremely useful for: (1) identifying suspicious transactions that might indicate money laundering or other possible criminal activity; (2) evaluating the merits of any potential criminal cases; and (3) tracing, analyzing, or identifying the disposition of proceeds from any illegal activity.

Question 6: Currently banks are required to file currency transaction reports for cash transactions in excess of $10,000. Is that an appropriate threshold amount, or should the amount be higher or lower?

Answer: Our work to date indicates that the threshold amount is probably appropriate for individuals but that consideration might be given to increasing the amount for businesses. In our opinion, individuals dealing in such large volumes of currency are the exception rather than the rule and merit reporting. Certain types of businesses, however, routinely deal with large amounts of cash that almost always exceed the threshold. Current Treasury regulations already permit banks to, in effect, increase the threshold for certain types of businesses under exemption procedures. However, we have found that the exemption process is not used to a large extent. Consequently, our current work is assessing whether efforts need to be made to increase the use of existing exemption procedures in addition to considering the dollar threshold for reporting.

Question 7: Banks are currently encouraged to file suspicious transactions reports with law enforcement and regulatory authorities. Are the forms useful to law enforcement agencies? Do law enforcement agencies use these reports in a manner which maximizes their utility?

Answer: On the basis of our initial observations, there appears to be considerable duplication in how suspicious transactions are reported which could significantly detract from the utility of these reports. Banks can report suspected money laundering or currency violations either on a CTR with the "suspicious transaction" block checked, through a Criminal Referral Form or both. It is our understanding that a third form is also being used for banks in the western part of the United States and that some states are using their own forms. Finally, some banks are simply reporting their suspicions on the phone to the local IRS office.

Question 8: A large number of the currency transaction reports filed are for certain customers, such as grocery and department stores, which routinely deposit large amounts of cash. What is the value of these forms to preventing money laundering? Should the Treasury attempt to reduce or eliminate the filing of reports on these routine transactions?

Answer: Law enforcement and regulatory officials we have spoken with agree that CTRs filed on large retail businesses that normally deal with large amounts of cash are of minimal value in detecting

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potential money laundering cases. IRS officials have estimated that between 30 and 40 percent of the CTRs filed are for these routine deposits which could have been exempted by the bank. (See question 6). We have been told, however, by Treasury and banking industry spokespersons, that most banks are reluctant to use the exemption authority. Because there are over 50 million CTRs stored on Treasury computers--a number that could double in 4 years at current filing rates--we believe that Treasury has a strong incentive to reduce the volume of reports. Consequently, if Treasury cannot encourage more banks to use the exemption procedures, it might consider the alternative of issuing exemptions itself.

Question 9: You testified that section 132 of FDICIA, relating to management standards, should apply to all institutions regardless of asset size. Does section 132 require institutions to develop standards for activities in which they do not engage, or in which they engage only incidently or infrequently?

Answer: The point of section 132 is to have banks follow sound procedures in their principal operations, such as making loans. The draft regulations that have been prepared by the FDIC and the Federal Reserve go right to the heart of the day to day activities that most affect the safety and soundness of banks, such as underwriting standards, internal controls, and loan documentation.

Questions from the Honorable Jim Bacchus for
Mr. Donald Chapin, Assistant Comptroller General
General Accounting Office

Question 1: Please compare the state of supervision of the thrift industry in the early 1980s with the current state of supervision of the banking industry. What similarities and differences exist? Please set out the financial conditions of the respective industries (for the thrift industry then and for the banking industry now). How do their capital levels and capital trends compare? What are the number of, and percentage of, financial institutions which are currently undercapitalized?

Answer: Deregulation in the 1980s provided expanded powers for thrifts and resulted in greater risk-taking in their operations, while regulatory oversight was reduced. Thrifts were empowered with broader lending opportunities and both banks and thrifts were given freedom to set interest rates to attract deposits. At the same time, regulators were given more flexibility in their approach to examining institutions during a time of major operational changes in the bank and thrift industries. Deposit insurance coverage was also increased from $40,000 to $100,000 and regulators' examination staffing levels were reduced during the early 1980s. Weak supervision of the thrift industry was a major factor in the failure of hundreds of savings and loans during the 1980s that led to the insolvency of the insurance fund.

Our recent reviews of both bank and thrift examinations[1] showed the examinations were too limited to fully identify and determine the extent of deficiencies affecting safety and soundness. The limitations we identified impeded early warning of the seriousness of bank and thrift weaknesses and reduced the opportunity for taking timely corrective action and minimizing losses to the insurance funds.

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[1] Bank and Thrift Regulation: Improvements Needed in Examination Quality and Regulatory Structure (GAO/AFMD-93-15, February 16, 1993), Bank Examination Quality: OCC Examinations Do Not Fully Assess Bank Safety and Soundness (GAO/AFMD-93-14, February 16, 1993), Bank Examination Quality: FRB Examinations and Inspections Do not Fully Assess Bank Safety and Soundness (GAO/AFMD-93-13, February 16, 1993), Bank Examination Quality: FDIC Examinations Do Not Fully Assess Bank Safety and Soundness (GAO/AFMD-93-12, February 16, 1993), and Thrift Examination Quality: OTS Examinations Do Not Fully Assess Thrift Safety and Soundness (GAO/AFMD-93-11, February 16, 1993).

Regarding industry conditions, thrift industry data as of June 1985 showed that 833 thrifts (24 percent) had capital levels of between zero and 3 percent. As of June 1993, only 47 thrifts (3 percent) had capital of less than 4 percent. As of June 1993, 97 percent of banks were well capitalized and less than 1 percent were undercapitalized As you know, many failed thrifts and banks have been resolved by the regulators in the late 1980s and early 1990s. Extraordinary interest rate spreads in 1992, continuing into 1993, are also a major factor contributing to the improved conditions of the banking and thrift industries.

Flawed corporate governance, including weak internal controls, was a common significant contributing factor to the large number of banks and thrifts that failed in the late 1980s and early 1990s. FDIC A provides a structure to strengthen corporate governance and facilitate early warning of safety and soundness problems. Such implementation of FDICIA and improved examinations and accounting rules are vital to regulatory effectiveness and protection of the insurance funds.

Question 2: Given the fact that Federal banking regulatory resources are limited (as is the case in most organizational structures, both government and private), where should such regulatory resources be focused? Would it not be more appropriate to focus regulatory efforts on troubled institutions (a point clearly established when Congress passed the early intervention provisions of FDICIA)? Do not federal regulators retain other methods of identifying problems at healthy institutions (e.g., call report information on asset growth or capital conditions, annual examinations sanction authority) to adequately protect the Federal Deposit Insurance funds from insolvency?

Answer We believe that regulatory resources should be focused on proactive approaches to examination and supervision for healthy institutions and, necessarily also on reactive approaches for troubled institutions. Evaluation of an institution's system of internal controls is a proactive regulatory approach, as it enables regulators to identify weaknesses at an early, correctable stage, before significant, irreversible financial deterioration results. For example, an evaluation of internal controls may determine that an institution does not have adequate controls over the monitoring and reporting of derivative activities. Identification of this weakness at an early stage would likely result in corrective action being taken before serious losses were incurred by the institution. Without an evaluation of controls, the weakness may not become evident until after the losses have already occurred.

The FDIC Improvement Act's requirements for assessments and reports on internal controls by management of the institution and its external auditors provide regulators with an efficient and effective mechanism to evaluate internal controls. With appropriate review of the management and auditors' reports, the regulators can focus their examination and supervision efforts on the most problematic areas of the institution The natural outcome of this approach is that well managed institutions with strong systems of control will require less examination and supervision efforts while troubled institutions with poor controls will require more In addition, this approach helps keep healthy institutions healthy by focusing on preventing, rather than ust detecting, unsafe and unsound activities which ultimately could cause an institution to deteriorate and fail.

Call report data are needed to monitor institutions' condition and performance between examinations, but they are not a substitute for on-site reviews of operations For example, the effectiveness of internal controls the quality of loans, and other factors critical to banking operations must be reviewed at the institution

Question 3: Please describe all regulatory authority available to Federal banking regulators other than that provided under Section 132 of FDICIA. Do Federal banking regulators retain adequate supervisory authority, on a case-by-case basis, to effectively supervise financial institutions without the implementation of Section 132 of FDICIA? If Section 132 were repealed, or applied only to troubled institutions as provided in H.R 962, what regulatory authority would be taken away from federal regulators in combatting problems at financial institutions on a case-by-case basis? Please be specific in your answer

Answer: We do not disagree that regulators had authority to deal with problem institutions before Section 132 was enacted, and that they would continue to have that authority if 132 is repealed. As we see it, the real issue concerns the effectiveness and timeliness of supervisory action.

In various GAO reports, which were cited in our statement to the Subcommittee, we pointed out that regulators were aware that there were serious problems in banks, but didn't take forceful action until it was too late. They did this because they felt that they had to see substantial deterioration of capital before they took action. Also, there was not a consistent understanding by either bank management or regulators of what standards were expected.

Section 132 addresses these problems and therefore should not be repealed or applied only to troubled institutions Section 132 makes it easier for the regulators to act on a timely basis in two respects. First, it establishes the connection in law between safety and soundness on the one hand and good management systems on the other When the Section 132 regulations are issued, the standards (or expectations) will be established and both bank managers and regulators alike should have a common understanding of the importance of the quality of risk management systems. Second, by testing the quality of these systems, regulators can quickly gain knowledge of whether the bank is being run in a safe and sound fashion. If problems are identified, the regulators can then use the authority they have to deal with the facts of the situation on a case-by-case basis Repealing Section 132 or applying it only to troubled institutions, would effectively diminish the regulators ability to identify and correct situations before they develop into real problems and losses to the deposit insurance funds. Section 132 provides the criteria or definitions of what constitutes a safe and sound banking practice or condition, which will be critical for regulators to use in implementing their prompt corrective action authority. Under FDICIA, the regulators can reduce a bank by one capital level if it is not operating in a safe and sound manner, such a reduction in turn could trigger other supervisory actions.

Question 4: Does the imposition of the various regulatory requirements on financial institutions pursuant to FDICIA involve cost to financial institutions? Please estimate the cost As part of your response please set out a summary of existing studies which attempt to quantify the cost of banking regulation.

Answer: For all banks there will no doubt be some start up costs to implement FDICIA. However for banks that already have good management and auditing systems, these costs should not be very great over the long haul. Furthermore, as FDICIA takes effect, there should be some offsetting savings for many banks--not only in lower deposit insurance premiums, but also improved efficiency and effectiveness of management systems, and reduced auditing and examination expenses resulting from properly functioning management systems. In addition, the corporate governance requirements of Section 112 of FDICIA (management and auditor reporting and audit committee requirements) are now only applicable to banks and thrifts with assets of $500 million or greater--approximately 1,000 institutions. FDIC's regulations exempted additional institutions than the smaller institutions exempted by FDICIA. FDICIA provided a threshold of $150 million or more in assets and allowed FDIC the flexibility to raise the threshold, which it did in issuing regulations.

pointed out in our testimony, we have a study underway that
tended to develop greater understanding of regulatory burden
s, including the basis for estimating both the costs and
lts of regulation. We have found that it is very difficult
nd reliable data on costs because banks keep their records in
rent ways, and it is hard to take adequate account of how
incurred today to comply with regulations may be offset by
ed future costs resulting from improved management systems and
loan losses.

Questions from the Honorable Bill McCollum for
Mr. Donald Chapin, Assistant Comptroller General
General Accounting Office

Question 1: H.R. 962 has a variety of diverse provisions affecting the regulatory burden on financial institutions. Please state which provisions of the bill that GAO can support.

Answer: In response to this question and to the request made by Chairman Neal and Congressman Bacchus, we are providing as Enclosure IV, our views on each provision of H.R. 962 where we have sufficient information to provide a response.

Question 2: How many healthy institutions has the GAO examined in preparation of its reports on banking supervision? How many healthy institutions have been examined by GAO on the adequacy of their internal controls? Please provide the number of thrifts, and the number of banking institutions examined in each case. What percentage, respectively, of the banking and thrift industries does this represent?

Answer: The question does not cite a specific report and GAO has conducted a number of studies related to bank supervision as shown by the listing of reports and testimonies submitted for the hearing record. In doing our work, we do not "examine" banks, but rather review the work of the regulators in conducting their supervisory and examination responsibilities. For example, in our recent review of bank and thrift examinations,[1] we reviewed a random sample of 58 bank and thrift examinations performed by the Office of the Comptroller of the Currency, Federal Reserve Board, Federal Deposit Insurance Corporation, and Office of Thrift Supervision. The random sample was taken from the universe of open banks and thrifts as of September 30, 1990 and included 20 banks with assets greater than $10 billion, 18 banks with assets less than $10 billion, and 20 thrifts of various sizes.

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[1]BANK AND THRIFT REGULATION: Improvements Needed in Examination Quality and Regulatory Structure (GAO/AFMD-93-15, February 16, 1993), BANK EXAMINATION QUALITY: OCC Examinations Do Not Fully Assess Bank Safety and Soundness (GAO/AFMD-93-14, February 16, 1993), BANK EXAMINATION QUALITY: FRB Examinations Do Not Fully Assess Bank Safety and Soundness (GAO/AFMD-93-13, February 16, 1993), BANK EXAMINATION QUALITY: FDIC Examinations Do Not Fully Assess Bank Safety and Soundness (GAO/AFMD-93-12, February 16, 1993), and THRIFT EXAMINATION QUALITY: OTS Examinations Do Not Fully Assess Thrift Safety and Soundness (GAO/AFMD-93-11, February 16, 1993).

For each institution in our study, we reviewed in detail the working papers supporting the most recent safety and soundness examination conducted by the regulators to assess the quantity and quality of evidence that supported conclusions in examination reports. The statistical nature of our study allowed us to project our results to the applicable universe of examinations covered by our work.

Our review of the 58 randomly selected bank and thrift examinations disclosed that regulatory examinations were too limited to fully identify and determine the extent of deficiencies affecting safety and soundness. These limitations impeded early warning of the seriousness of bank and thrift weaknesses and reduced opportunity for taking timely corrective action and minimizing losses to the insurance funds. One of the primary weaknesses we found in our examination review was a lack of comprehensive internal control assessments by regulators.

A strong system of internal controls provides the framework for the accomplishment of management objectives, accurate financial reporting, and compliance with laws and regulations. Effective internal controls serve as checks and balances against undesired activities and, as such, provide reasonable assurance that banks and thrifts operate in a safe and sound manner. The lack of good internal controls puts insured depository institutions at risk of mismanagement, waste, fraud, and abuse.

In previous reports, we cited weak internal controls as contributing significantly to the failure of banks and thrifts.[2] A major focus of these reports was to analyze the causes of bank and thrift failures, as cited by regulators, as a basis to determine what, if any, actions could be taken by regulators or others to help avert future bank and thrift failures. Weak internal controls was a common theme identified by regulators in their reviews of these failures. Based on this finding, we undertook our review of bank and thrift examinations described above to, among other things, assess the adequacy of the regulators' reviews of internal controls. We identified a number of weaknesses as indicated by the report titles. We recommended, among other corrective actions, that bank and thrift regulatory

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[2]FAILED BANKS: Accounting and Auditing Reforms Urgently Needed (GAO/AFMD-91-43, April 22, 1991), BANK FAILURES: Independent Audits Needed to Strengthen Internal Control and Bank Management (GAO/AFMD-89-25, May 31, 1989), and THRIFT FAILURES: Costly Failures Resulted From Regulatory Violations and Unsafe Practices (GAO/AFMD-89-62, June 16, 1989).

agencies establish examination policies to perform annual comprehensive internal control reviews as part of the examination of all banks and thrifts using, where appropriate, the internal control assessments required by the FDIC Improvement Act or otherwise performed by the institution's management and its independent auditors.

Question 3: Judged by existing statistical standards for accuracy, are the financial institutions examined by GAO in formulating their conclusions on bank supervision statistically diverse and representative enough of the banking industry to draw conclusions on the appropriate level of regulation of healthy institutions?

Answer: As previously noted, GAO did not "examine" institutions in formulating its conclusions on bank supervision, but rather reviewed examinations performed by the bank and thrift regulators. Each of our reports contains detailed information on the scope and methodology of our work.

Question 4: Please comment on the appropriateness of applying conclusions drawn from an examination of a limited number of troubled or failed institutions to the 10,000 or so healthy financial institutions currently operating in the U.S.

Answer: As stated in our answers to questions 2 and 3 above, we have done extensive work in reviewing the quality of bank and thrift supervision and examination and in analyzing the safety and soundness weaknesses that contributed significantly to bank and thrift failures in the 1980s and 1990s. We believe the recommendations in our reports are well founded to protect the insurance funds and the taxpayers. Further, they directly benefit healthy institutions by minimizing losses from failed institutions for which healthy institutions have paid out billions over the past several years.

GAO Comments on H.R. 962
the Economic Growth and Financial Institutions
Regulatory Paperwork Reduction of Act of 1993

Section 101 - Regulation of Real Estate Lending

This provision would require regulators to minimize the negative impact that the standards on real estate lending mandated by FDICIA would have on real estate lending, consistent with safety and soundness.

In principle we have no objection to the provision because we believe there is no inherent conflict between maintaining safety and soundness standards and the provision of adequate credit to the economy. There is a risk, however, that enactment of this provision might be taken as a signal that regulators should put to one side the lessons about the importance of good underwriting standards that should be evident from the excessive real estate losses incurred by both banks and thrifts in recent years.

Section 102 - Real Estate Appraisal Amendment

This provision would direct the Appraisal Committee to encourage states to develop reciprocity agreements to allow appraisers qualified in one state to perform appraisals in another.

Although we cannot comment on the need for this provision, in principle efforts to assure an adequate supply of qualified appraisers make sense.

Section 954 of the Housing and Community Development Act of 1992 requires that GAO study and report by April 1994 and again by October 1995 on the adequacy and quality of appraisals and evaluations for real estate transactions below the threshold level (currently $100,000). The study is to consider (1) the cost to the bank, (2) the possibility of loss to the insurance fund, (3) cost to the customer, and (4) effect on low income housing. The study may provide some insights on the impact of the availability of appraisers on the appraisal process.

Section 111 - Audit Costs

Section 111(a)(1) - Auditor Attestations - would eliminate the requirement that a financial institution's independent public accountant attest to and report on management's assertions on internal controls. It would also eliminate the requirement that the independent public accountant apply agreed upon procedures to

objectively determine the institution's compliance with designated laws and regulations.

We oppose this provision as independent reviews are necessary to check management's assertions and comprehensive reviews of internal controls are not currently being performed by examiners. Independent public accountants have the ability to review internal controls of complex financial systems. FDIC has stated that over 96 percent of the institutions covered by the applicable regulations already have an annual financial audit. Reviewing internal controls is a component of a financial audit and, therefore, the independent public accountant can efficiently review management's assertions as part of the audit.

Section 111(a)(2) - Duplicative Reporting - would allow holding company subsidiaries regardless of size or CAMEL rating to satisfy the requirements contained in Section 112 of FDICIA at the holding company level if comparable services and functions are provided at the holding company level.

We oppose this provision. Many of the banks that would be affected by the change are large enough that their individual failures could seriously impact the Bank Insurance Fund and may have potential rippling effects throughout the Nation's financial system. The FDICIA internal control and audit committee requirements were designed to ensure an effective corporate governance system for those large institutions which pose such risks.

Existing provisions of the act already provide an exemption for institutions with assets less than $5 billion, and for institutions with assets greater than $5 billion but less than $9 billion that have a 1 or 2 CAMEL rating. We believe these exemptions are reasonable. However, without an independent audit committee for the large institutions, coupled with no requirement to report on the effectiveness of internal controls and compliance with safety and soundness laws and regulations, we are concerned that appropriate management oversight will not extend to all large banks within the holding company structure. Therefore, we believe that the largest institutions should continue to be required to meet the corporate governance requirements separately because of the exposure which these individual institutions present to the taxpayers, shareholders, and uninsured depositors.

Section 111(a)(3) - Independent Audit Committees - would modify the audit committee provisions contained in FDICIA, requiring only a majority (rather than all) audit committee members to be outside directors. It would also remove the provision prohibiting "large customers" from serving on the audit committees of institutions

designated as "large" by FDIC. In addition, Section 111(a)(3) would require each federal banking agency, by regulation, to exempt from the audit committee requirements contained in FDICIA institutions that "face hardships in retaining competent directors on their internal audit committees."

We oppose these provisions. Audit committees are intended to play a very important role in the corporate governance of financial institutions. Their responsibilities should include monitoring internal controls and ensuring that management is not overriding internal controls, supervising the activities of internal and external auditors, and reviewing financial statements and important accounting policies. Audit committees need to be made up of independent outside directors to enable an impartial review of management's conduct of business In that respect, FDICIA provides that large customers of large institutions are not to serve on the committees. FDIC has defined a "large institution" as one with assets of $3 billion or more. With that threshold, fewer than 2 percent of the nation's institutions would be defined as "large."

Section 111(a)(4) - Public Availability - would authorize FDIC and the other federal banking agencies to designate certain information privileged and confidential and not available to the public, notwithstanding the FDICIA requirement that institutions' annual reports be made available for public inspection

We oppose this provision as we believe that uninsured depositors, shareholders, and others at risk are entitled to information about the institution's management and financial condition. As required by FDICIA, the annual report is to contain the institution's annual financial statements and the auditor's opinion; a statement of management's responsibilities for preparing financial statements, establishing and maintaining an adequate system of internal control, and complying with designated laws and regulations; management's assessment of the effectiveness of internal controls and the institution's compliance with designated laws and regulations; and the independent public accountant's report on management's assertions on internal controls Such information provides for public accountability of management's stewardship for those at risk.

Section 111(a)(5) - Quarterly Reports - would require FDIC to provide prompt written notice to institutions whose quarterly reports will be subject to independent public accountant review under provisions contained in FDICIA.

We agree with providing timely notice to such institutions.

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Section 111(b) - Effective Date - would make the provisions contained in Section 112 of FDICIA applicable to institutions for fiscal years beginning after December 31, 1993, rather than December 31, 1992.

We oppose this provision. The FDIC has issued implementing regulations and the AICPA has issued auditing standards for auditor reporting on internal controls. The FDIC issued regulations and guidelines that allow the approximately 1,000 institutions subject to Section 112 considerable flexibility in implementing the requirements. The FDIC sought public comment on proposed regulations in September 1992 and the final regulations were significantly revised from the draft to respond to comments. We see no reason to delay implementation.

Section 112 - Recourse Agreements

This provision would require that GAAP accounting be used in determining the necessary capital to be held against loans sold with recourse.

Section 121 of FDICIA allows the regulators to adopt more stringent standards than GAAP to meet the objectives set forth in Section 121 With increased securitization of assets by banks, the question of the appropriate amount of capital that should be required for such arrangements is an important issue. In this area, as in most other areas of capital regulation, regulators need to have flexibility provided by Section 121 in determining how applicable capital standards should be calculated to be sure that the standards can be kept current with market developments.

Section 113 - Market Value Accounting

Section 113 would eliminate the requirement contained in FDICIA that federal banking agencies jointly develop a method for insured depository institutions to provide supplemental disclosure of the estimated fair market value of assets and liabilities, to the extent feasible and practicable, in balance sheets and other financial statements and reports.

We oppose this provision. As stated in our testimony in more detail, we believe disclosure of the fair value of assets and liabilities is information that regulators need to fully understand the financial condition and activities of banks and thrifts. The FDICIA requirement parallels current accounting rules although it extends fair value disclosures to nonfinancial assets and liabilities. Exceptions are permitted by current accounting rules and FDICIA when it is not practicable to estimate fair value.

FDIC has not yet issued final regulations. We believe that the final regulations should require that reports submitted by institutions to the regulators that do not disclose fair market values for reasons of practicality explain what information was considered and why it is not feasible to estimate fair value.

Section 114 - Report on Capital Standards and Their Impact on the Economy

This provision would require Treasury to report to Congress on the impact of risk-based capital standards on safety and soundness, availability of credit, and economic growth no later than 90 days after enactment of H.R. 962.

A study of the impact of risk based capital standards could be beneficial, although the study could be performed without special legislation. We question, however, how much new information can be obtained in a 90 day study. If such a study is authorized, it would be appropriate to seek (1) to assess the competitive effects in world markets that have resulted from implementation of the standards around the world, and (2) to place the significance of the standards in the context of other factors affecting bank condition, credit, and economic growth. A one year deadline is reasonable for such a study.

Section 115 - Minimize Potential Impact of Capital Standards on Credit Availability

This provision would delay implementation of the interest rate risk capital standard contained in Section 305 of FDICIA, phasing in such implementation to correspond to the implementation of a similar standard internationally. It would also repeal the provisions in Section 305 of FDICIA that require bank regulatory agencies to develop capital standards to account for market concentration risk and risks in non-traditional activities.

We oppose this provision.

The nature of risks associated with interest rate risk are well known and can be quantified to a reasonable degree. The regulations drafted by the agencies are designed to minimize the burden on well managed institutions by allowing such institutions to make use of their own systems for monitoring exposure to interest rate risk in complying with the requirement. Measuring risk and requiring an allocation of capital in this area can help to strengthen banks, and it can also eliminate a potential regulatory incentive for banks to invest in securities rather than make loans.

We understand the problems of trying to develop measures of concentration risk and the risk of non-traditional activities, but the effectiveness of Section 305 does not require quantitative measures of these risks. In our view, this part of Section 305 should be retained because it properly focuses the attention of bank management and regulators on areas which have proven to be sources of problems for banks in the past. We also believe that the provision will put little burden on well run institutions

We believe the Congress should be concerned with the delay that has occurred in implementing Section 305. The statute provided for final regulations to be published by June 1993, and this has not occurred. At present only proposed regulations for interest rate risk have been officially published for comment by the bank regulators. If the banking system is to be operated in a safe and sound manner in today's highly competitive financial markets, it is essential that appropriate measures of capital be defined and enforced. Effective implementation of Section 305 is an important part of modernizing the regulations that apply to insured depository institutions.

Section 122 - Culpability Standards for Outside Directors

This provision would remove a disincentive for outside directors to serve on boards of directors by modifying culpability standards required for imposition of certain levels of regulatory civil money penalties.

We do not support this provision. An outside director has an important and unique fiduciary responsibility to the financial institution served. In that capacity, the director is basically responsible for knowing that the institution is operating in a safe and sound manner. To effectively reduce the outside director to have to act knowingly or recklessly" to be deemed culpable as this proposal would do, ironically could provide an incentive for the director to not be apprised of questionable bank activities. The ability of banks to attract capable outside directors is an important area of concern, but we do not believe this provision is the solution

Section 131 - Regulatory Appeals Process

This provision would direct the regulators to establish a regulatory appeals process to permit review of regulatory determinations.

We support an appeals process and have done so when proposed by an interagency initiative discussed at the National Examiners

Conference in Baltimore, Maryland, in December 1992. That proposal properly, in our view, required the independence of the appeals officer. It also clearly stated that an appeal could not be used to delay, thwart, or rule on a proposed administrative or enforcement action; disputes about such actions could only be pursued through existing administrative or judicial processes.

We objected to the confidential nature of the agency initiative under which the appeals officer would not apprise the examiner of an appeal. That approach could jeopardize the appeals officer's ability to render a fair opinion by making it more difficult for that officer to get perspectives on the fact pattern underlying the dispute from both the banker and the examiner.

While we have not assessed the adequacy of the agencies' appeals processes established pursuant to this interagency initiative, we understand each agency has established a process--which may reduce the need to legislate an appeals process.

Section 132 - Aggregate Limits on Insider Lending

This provision would statutorily establish that all banks under $100 million in deposits may lend to all insiders, in the aggregate, up to two times unimpaired capital and surplus. It would also provide the Federal Reserve Board with the authority to make exceptions to this lending cap by regulation, permitting banks under $250 million in deposits to lend in the aggregate to insiders up to two times unimpaired capital and surplus.

Based on a comprehensive study we are completing on insider activities, we cannot support a provision to relax current aggregate lending limits on extensions of credit to insiders. The existing limits already provide for the Federal Reserve to set a higher limit, not to exceed 200 percent of unimpaired capital, for smaller banks which may otherwise have difficulty attracting directors. Our study will show that insider-related problems were a major contributing factor in about 25 percent of the banks that failed in 1991 and 1992. Prior to their failure, these banks were cited by federal bank regulators for many violations of insider regulations. The most frequently-cited violation was exceeding aggregate lending limits (which at that time related to individual borrower lending limits). Furthermore, our study found a strong association between insider violations and the larger problem of poor overall bank administration by management and poor oversight by bank boards of directors. We therefore recommend that, rather than concentrate on specific violations of insider regulation, or on the relaxing--or

tightening--of current insider lending limits, banks and regulators view insider problems more broadly, and seek to determine whether they are indicators of deeper management and oversight problems at a bank.

Section 133 - Sterile Reserves Study

This provision would require the Federal Reserve, in consultation with the FDIC, to study the necessity for continuing to require insured depository institutions to maintain sterile reserves and to pay interest on such reserves The OMB and CBO are also directed to report to Congress on the budgetary impact of such payments of interest.

We support this study.

Section 134 - Credit Card Accounts Receivable Sales

This provision would require undercapitalized insured depository institutions to notify the FDIC in writing before entering into an agreement to sell credit card accounts receivables It would also grant FDIC the discretionary authority to waive its right of repudiation on credit card accounts receivables sales made prior to insolvency

In general, we would support allowing an undercapitalized institution to raise its capital levels through the sale of credit card receivables provided that FDIC is provided an opportunity to review the agreement in advance and waive its rights to repudiate this agreement should the institution fail

While the proposal in H.R. 962 may facilitate such sales by assuring the market that FDIC will not repudiate an agreement, there are some coordination difficulties that may arise among the regulators. In many cases FDIC may not have knowledge of a bank's condition or be in a position to assess the agreement in relation to the safety and soundness of the bank. On the other hand, OCC or the Federal Reserve--the primary regulators--who would be in such a position--quite properly do not have the authority to repudiate a contract at failure. Consequently, without its own independent assessment, FDIC may not be willing to waive its rights. If so, this provision would be rendered moot.

Section 135 - Changes to the Federal Home Loan Bank Act to Promote Credit Availability

This provision would increase the amount of credit available by: (a) expanding the amount of non-residential and residential real estate-related collateral that can be used to secure FHLBank advances; and (b) giving the FHLBanks the authority to purchase and invest in participation interests in residential construction loans originated by member institutions, and to enhance the credit quality of any of these interests that the FHLBanks resell.

We see no reason to broaden the types of collateral that can be used to secure advances. We believe the present collateral base is fully adequate to secure advances. For example, in 1992 FHLBank members held about $760 billion in assets which could be pledged as collateral for FHLBank advances. Simultaneously, members held approximately $80 billion in advances. Thus, the collateral base seems to be large enough to support reasonable advance activity.

We believe that the FHLBank System should not increase the risk it bears in undertaking new activities unless such activities would bring substantial and obvious economic benefits to the System and its customers while furthering the System's mission. To that end, we have identified several criteria to apply in assessing proposed new activities for the System. Our proposed criteria require, among other things, that a new activity not put a FHLBank in competition with its members, that FHLBanks have the expertise needed to assess the associated risks, and that a new activity add value by addressing a need not currently met by the market. Making or offering credit enhancements on residential construction loans fails each of these criteria and thus we believe such activity would be inappropriate for FHLBanks. Notably, a study committee representing the System's member/shareholders reached the same conclusion in their recent report to Congress. Finally, the Independent Bankers Association of America testified earlier this year that housing construction credit needs are being adequately met by the private sector, and several FHLBank presidents have told us that such lending carries substantial risk and would not be appropriate for the System.

Section 201 - Regulatory Standards

This provision would substantially scale back Section 132 of FDICIA. It would require regulators to prescribe safety and soundness standards only for those institutions that are not at least adequately capitalized with a CAMEL rating of 1 or 2. It would further authorize regulatory agencies to waive the applicability of Section 132 on a case-by-case basis.

We oppose this section.

Section 132 is an important part of modernizing the system of bank regulation and supervision. The standards contained in the section simply reflect the need to be sure that all insured depository institutions have the risk management systems they need to operate safely and soundly in today's competitive, deregulated financial markets. Section 132 of FDICIA is important and should be retained because it gives the regulators both the mandate and the authority to direct their attention to the adequacy of banks' risk management systems.

Section 132 is also crucial to successful implementation of the prompt corrective action provisions of FDICIA. The prompt corrective action mandate, whereby the regulators are obligated to close insolvent institutions before their capital is exhausted, protects the interests of the deposit insurance fund and of healthy banks that otherwise would have to pay higher premiums to pay for insurance losses. Banks are highly leveraged institutions, and a bank's failure to adequately manage its exposure to credit or market risks can quickly erode its capital. Furthermore, our studies have shown that falling capital levels are a lagging indicator of problems in a bank. To protect the fund from losses, therefore, the regulators must be prepared to act when serious deficiencies become apparent in the systems a bank uses to monitor and control risks.

Section 132 has been widely misunderstood to call for highly detailed and restrictive rules that all banks must follow. FDICIA does not require this, and we see no reason to assume that the agencies would implement the act in such a fashion. The draft regulations that have been proposed by the banking agencies call attention to the importance of key management controls but also make it clear that rigid requirements will not be imposed on the banks.

Supervisory manuals and agency directives have long provided examiners with guidelines and criteria for evaluating banks in areas such as underwriting standards that are specified by

Section 132 of FDICIA. Rather than creating a burden, we think it will be salutary for banks to understand more specifically the standards regulators will use in examining their institutions and what the consequences will be in given situations For the most part, well capitalized, well run banks have recognized the importance of good management systems and have developed their own standards in many of these areas For such banks, there should be no real burden because their systems should generally already be consistent with standards required by regulation.

In view of the importance of Section 132 for modernizing the way banks are regulated and supervised, delays in implementing this section should be of great concern to the Congress. Although the act stated that regulations were to be published in August 1993, they have not yet been published. The standards contained in Section 132 are to go into effect in December 1993.

Section 202 - Paperwork Reduction Review

This provision would direct federal regulators to review the impact that current written policy requirements have on banks, and to reduce these requirements where appropriate not later than 180 days after enactment of H.R. 962.

We support the objective of this provision, although legislation should not be needed for the agencies to continuously pursue this objective. Under credit availability initiatives of both the Bush and Clinton Administrations, a similar charge went out to the regulatory agencies to reduce unnecessary regulations and requirements. Another comparable effort was undertaken by the agencies as part of the FDICIA-mandated regulatory burden studies. With the extensive requirements on the books, more than 6 months may be needed to do an in-depth thoughtful study. We are currently doing a review for the Senate Banking Committee on regulatory burden that will be completed by the end of the year.

Section 203 - Rules on Deposit Taking

This provision would change a provision in current law which places restrictions on the interest rates that adequately capitalized banks may provide on deposits.

We oppose this provision.

One of the problems that both banks and thrifts ran into in the recent past is that relatively weak institutions would out bid healthy ones for funds. At the present time the vast majority of banks meet the well capitalized definition, and we see no basis for

going back to a situation which in essence enables banks that meet a lesser standard to take advantage of the federal deposit insurance guarantee by bidding aggressively for funds.

Section 204 - Transition Period

This provision would create a general statutory provision that, unless emergency circumstances exist or directed otherwise by Congress new regulations requiring additional reporting, disclosure or other procedures by banks could not be phased in sooner than 180 days after becoming final.

We agree that adequate transition periods should be built into new regulatory initiatives. The past several years have, of course, seen large numbers of changes in regulation and it can be hoped that we will soon reach a period where less frequent revisions are needed to keep the regulatory system current with market developments.

Section 301 - Annual Examinations

Section 301(a)(1) - Small Institution Treatment - would eliminate the current exception to the annual examination requirement (18 month rule) for certain well capitalized insured depository institutions with less that $100 million in assets. It would instead authorize examinations every two years for well capitalized institutions with assets of less than $250 million that are well managed, and not currently subject to a formal enforcement order. In addition, the two year exception would not apply where any person has acquired control of the institution during the 12 month period in which a full-scope, on site examination would generally be required, but for the exception.

We oppose extending the interval between examinations. We believe that annual safety and soundness examinations are needed to timely detect unsafe and unsound conditions, such as internal control weaknesses before they result in deterioration of asset quality and erosion of capital On-site review is necessary to detect such weaknesses Even if controls are found to be effective at a point in time, such favorable conditions cannot be assumed for the future.

Section 301(a)(2) - State Examinations - would allow the substitution of a state examination for a federal examination whenever the appropriate federal banking agency determines that such an examination carries out the purposes of the law, instead of in alternate 12 month periods as provided by Section 111 of FDICIA.

We support effective use of state examinations, but believe the current alternate 12-month interval is best maintained to ensure that the federal regulators' knowledge of the institutions is not eroded. However, we believe that, to the extent practicable, use should be made of state examinations in planning federal examinations

Section 301(a)(3) - Certain Depository Institutions Within Holding Companies - would authorize federal banking agencies to exempt subsidiary insured depository institutions from the annual examination requirement if (a) the holding company structure has adequate controls or (b) the insured depository institutions owned or controlled by the holding company which hold a substantial majority of total assets have been examined under the annual examination requirements.

As previously stated, we support annual examinations of insured depository institutions However, the conditions described by the proposal should be considered in determining the scope of the examination of depository institutions within the holding company structure.

Section 302 - Coordinated Examinations

Section 302(a Coordinated State and Federal Examinations - would require all federal banking agencies to coordinate all examinations at an insured depository institution and to work with other federal and state bank supervisors to coordinate examinations so as to minimize the disruptive effects of such examinations on institution operations.

We support this provision. Our February 16, 1993, report Bank and Thrift Regulation: Improvements Needed in Examination Quality and Regulatory Structure (GAO/AFMD-93-15) discusses the need for effective use and coordination of examinations.

Section 303 - Differences in Accounting Principles

Section 303 would require each agency to require insured depository institutions to use accounting principles consistent with GAAP to the extent practicable so as to minimize differences between statements and reports, and thereby reduce the compliance burdens and costs on such institutions.

We believe Section 121 of FDICIA - Accounting Objectives, Standards, and Requirements - already essentially requires the consistent use of GAAP being proposed.

Section 304 - Reduction in Call Report Burdens

This provision would require regulators to review bank costs associated with the quarterly report and minimize the frequency and impact of changes.

We agree with the need to minimize the burden relative to call reports, especially to limit the frequency of changing call report data requirements since change itself is burdensome to affected institutions.

We have issued a report encouraging the regulators to proceed with their intentions to receive call report information through an electronic medium to reduce manual input and processing by banks and regulators Doing so may speed the availability of call report data to the public.

Section 305 - Regulatory Review of Capital Compliance Burden

This provision requires the Federal Financial Institutions Examination Council to conduct a regulatory review of whether compliance by community banks with the risk-based capital rules is unnecessarily costly and burdensome, and where appropriate, to reduce such costs and burdens

We agree with the need to be concerned with the impact of capital standards and other regulations on small banks, and the banking laws already make provision for excluding smaller banks from some provisions that are intended primarily for larger banks. The risk-based capital standards were primarily designed to apply to larger banks that had substantial off balance sheet commitments. The impact of these standards on the amount of capital that most smaller banks must hold is therefore likely to be small. Nevertheless it would be reasonable to look at whether there is an excessive administrative burden on smaller banks

As a technical matter authorizing the FFIEC to change the rules applicable to banks would give that coordinating body more authority than it now has in regulatory matters.

Section 305 of FDICIA requires the regulators to review the adequacy of bank capital standards every two years, and the requirement to pay particular attention to the effects on small banks could be included in that assessment.

Section 306 - Branch Closures

This provision would exclude certain entities from the definition of "branch" in the regulations concerned with branch closure requirements. Principal exclusions would be automated teller machines, and branches acquired through merger, consolidation, purchase, assumption or other method that is located in a local market currently served by another branch of the acquiring institution.

Since we are currently doing an extensive study of CRA for the House Banking Committee and the availability of banking services within an institution s lending area is a related issue, we will defer taking a position on this provision. Instead we will take it into consideration in our study.

Section 307 - Bank Secrecy Act

This section would require the Secretary of the Treasury to conduct an annual review of bank secrecy regulations and make several specific changes to reduce the burden of filing reports

We agree with the need to look at Bank Secrecy Act provisions, but there are already two mechanisms in place to accomplish the review that appears to be the intent of the first part of the section: a Treasury task force, and an advisory group established by statute in 1992 that has just recently been organized.

Some of the specific provisions for reducing the burden of Bank Secrecy Act reporting appear to have merit. We would prefer, however, to see consideration given to looking at the program as a whole rather than on a piecemeal basis. We note that more comprehensive legislation to do this is pending H R. 3235). It would, therefore, be appropriate to coordinate consideration of this section of H.R. 962 with that being given to the more comprehensive legislation.

Section 321 - Simplify Bank Holding Company Procedures

This provision would expedite procedures for acquiring control of a bank or reorganizing in which a person or group exchange shares in a bank for shares in a newly formed holding company

We understand the Federal Reserve, as part of its FDICIA-mandated regulatory burden study, has an initiative to simplify and expedite the bank holding company applications process. That initiative may effectively address the intent of this provision.

Section 324 - Reduction of Post Approval Waiting Period for Bank Holding Company Acquisitions

This provision would shorten the current 30 day waiting period during antitrust review of a bank holding company acquisition to as little as 5 days if no adverse comments have been received, and if the Attorney General concurs.

We have not studied the waiting period and thus have no comment on the language of the bill. Our work on interstate banking does indicate, however, that the ability to adequately enforce antitrust laws is an important element in making sure that consolidation does not unduly lessen competition in the banking industry.

Section 401 - Streamlined Lending Process for Consumer Benefits

This provision would require the Federal Reserve, in consultation with the Department of Housing and Urban Development, to conduct a study on ways to streamline the credit-granting process. The study is to be completed within 12 months of enactment of H.R. 962.

Should such a study be required to find ways to reduce the cost and time of home mortgage, small business, and consumer lending, we would suggest this be done on an interagency basis to ensure all regulatory perspectives are included, as well as HUD's, and to ensure secondary market perspectives are included. Additionally, industry or public comments may also better ensure that those affected have an opportunity to participate. The public comment period and process may cause the whole study to take more than 12 months.

Section 405 - Exemption for Business Accounts

This provision would amend the Truth in Savings Act to limit its application to accounts used by consumers primarily for personal, family, or household purposes.

We have done no work on Truth-In-Savings, but understand the Federal Reserve initiated a study prior to the FDICIA requirements' implementation in connection with its regulatory burden initiatives.

Section 411 - Availability Schedules

This provision amends certain requirements under the Expedited Funds Availability Act to allow more time to collect checks under certain circumstances. This would include requiring that funds from local checks be made available on the third day after deposit

rather than the second day, as required under current EFAA availability schedules.

In our earlier study on implementation of EFAA, the industry was unable to demonstrate its vulnerability to check fraud due to the proposed availability schedules, particularly relative to local check processing. Congress was not persuaded to change this schedule without evidence of this vulnerability. If any schedule change is considered, it should be crafted so that it is consistent with the intent of the original temporary and permanent schedules, i.e., in anticipation of technological and operational improvements to the check clearing processes. So, a temporary schedule change could possibly be considered contingent upon a more stringent permanent schedule at a prescribed time when the advances would likely be able to reduce fraud vulnerability.

Section 431 - Home Mortgage Disclosure Act Exemption

This provision requires annual adjustments to the exemption amount of assets based on changes in the Consumer Price Index.

We are including HMDA in our CRA study and will reserve comment until the study is completed in the spring of 1994.

Section 432 - Home Ownership Debt Counseling Notification

This provision would modify the current homeownership counseling provision to clarify that failure to comply with the counseling notification requirements will not affect foreclosure proceedings under state law and simplify the notice requirements.

We have no basis to comment now, although we are planning a study to look at various disclosure issues.

Section 442 - Exemption of Business Loans from RESPA

This provision would exempt business, commercial and agricultural loans, and loans to government agencies or instrumentalities, from RESPA.

Although we did not look into this in depth, our study of regulatory impediments to small business lending suggests that this provision would have merit.

Section 501 - Reduce CRA Burden/Increase Incentives to Low and Moderate Income Communities

This provision would modify the CRA to direct the regulators to reduce paperwork compliance burden, create a "safe harbor" provision, provide CRA credit for certain joint ventures, permit special purpose banks to comply in a manner which reflects the nature of their business, and eliminate redundant federal and state exams.

We will consider this provision in our CRA study to be completed in spring 1994.

GAO REPORTS AND TESTIMONIES SUPPORTING THE NEED FOR THE PROMPT REGULATORY, SUPERVISORY AND ACCOUNTING REQUIREMENTS OF FDICIA

REPORTS

BANK AND THRIFT REGULATION: Improvements Needed in Examination Quality and Regulatory Structure (GAO/AFMD-93-15, February 1993)

BANK EXAMINATION QUALITY: OCC Examinations Do Not Fully Assess Bank Safety and Soundness (GAO/AFMD-93-14, February 1993)

BANK EXAMINATION QUALITY: FRB Examinations and Inspection Do Not Fully Asses Bank Safety and Soundness (GAO/AFMD-93-13, February 1993)

BANK EXAMINATION QUALITY: FDIC Examinations Do Not Fully Assess Bank Safety and Soundness (GAO/AFMD-93-12, February 1993)

THRIFT EXAMINATION QUALITY: OTS Examinations Do Not Fully Assess Thrift Safety and Soundness (GAO/AFMD-93-11, February 1993)

DEPOSITORY INSTITUTIONS: Flexible Accounting Rules Lead to Inflated Financial Reports (GAO/AFMD-92-52, June 1992)

AUDIT COMMITTEES: Legislation Needed to Strengthen Bank Oversight (GAO/AFMD-92-19, October 1991)

BANK SUPERVISION: OCC's Supervision of the Bank of New England Was Not Timely or Forceful (GAO/GGD-91-128 September 1991)

FAILED BANKS: Accounting and Auditing Reforms Urgently Needed (GAO/AFMD-91-43, April 1991)

BANK SUPERVISION: Prompt and Forceful Regulatory Actions Needed (GAO/AFMD-91-69, April 1991)

DEPOSIT INSURANCE: A Strategy for Reform (GAO/GGD-91-26 March 1991)

BANK INSURANCE FUND: Additional Reserves and Reforms Needed to Strengthen the Fund (GAO/AFMD-90-100, September 1990)

THRIFT FAILURES: Costly Failures Resulted From Regulatory Violations and Unsafe Practices (GAO/AFMD-89-62, June 1989)

BANK FAILURES: Independent Audits Needed to Strengthen Internal Control and Bank Management (GAO/AFMD-89-25, May 1989)

TESTIMONIES

BANK AND THRIFT REGULATION: FDICIA Safety and Soundness Reforms Need to be Maintained (GAO/T-AIMD-93-5, September 23, 1993)

BANK AND THRIFTS: Safety and Soundness Reforms Need to be Maintained (GAO/T-AFMD-93-2, January 27, 1993)

BANK AND THRIFT REGULATION: Improvements Needed in Examination Quality and Regulatory Structure (GAO/T-AFMD-93-2, February 16, 1993)

CONDITION OF THE BANK INSURANCE FUND: Outlook Affected by Economic, Accounting, and Regulatory Issues (GAO/T-AFMD-92-11, June 30, 1992)

BANK SUPERVISION: Observations on the National Bank and Thrift Examiners' Conference (GAO/T-GGD-92-10, January 3, 1992)

OCC's Supervision of the Bank of the New England (GAO/T-GGD-91-66, September 19, 1991)

Deposit Insurance: A Strategy For Reform (GAO/T-GGD-91-12, March 7, 1991)

Accounting and Auditing Reforms are Urgently Needed and Essential to Any Plan for Recapitalizing the Bank Insurance Fund or Deposit Insurance Reform (GAO/T-AFMD-91-3, April 23, 1991)

RESOLVING FAILED SAVINGS AND LOAN INSTITUTIONS: Estimated Costs and Additional Funding Needs (GAO/T-AFMD-90-32, September 19, 1990)

Additional Reserves and Reforms are Needed to Strengthen the Bank Insurance Fund (GAO/T-AFMD-90-28, September 11, 1990)

Financial Condition of the Federal Deposit Insurance Corporation's Bank Insurance Fund (GAO/T-AFMD-89-15, September 19, 1989)

Resolving the Savings and Loan Crisis: Billions More and Additional Reforms Needed (GAO/T-AFMD-90-15, April 6, 1990)

PROPERTY AND CASUALTY INSURANCE: Thrift Failures Provide Valuable Lessons (GAO/T-AFMD-89-7, April 19, 1989)

FAILED THRIFTS: Internal Control Weaknesses Create and Environment Conducive to Fraud, Insider Abuse, and Related Unsafe Practices (GAO/T-AFMD-89-4)

First Interstate Bank

First Interstate Bank
of Texas, N.A.
P.O. Box 3326
Houston, TX 77253-3326
713 224-6611

October 1, 1993

The Honorable Carolyn Maloney
1504 Longworth House Office Building
Washington, D.C. 20515

Dear Congresswoman Maloney,

On September 23, 1993, I testified before the Subcommittee on Financial Institutions Supervision, Regulation and Deposit Insurance of the Committee on Banking, Finance and Urban Affairs regarding H.R. 962. During the question and answer session, you asked me if I knew the amount that First Interstate Bank of Texas, N.A. currently has invested in government securities. I promised you that I would provide you with that information upon my return to the bank.

Enclosed is the Consolidated Report of Condition and Income--FFIEC 031 for the close of business as of June 30, 1993. Please refer to Schedule RC-B on page RC-4 for a detailed breakdown of our bank-owned securities. The bank's total investment in securities can also be found in Schedule RC on page RC-1.

Thank you again for the opportunity to testify in favor of H.R. 962. If I may be of any more assistance to you or your staff, please do not hesitate to call.

Sincerely,

Dianne M. Lopez

Dianne M. Lopez
Senior Vice President and
Regional Compliance Manager

c: The Honorable Stephen Neal,
House Banking Committee

Vickie Stallings, Executive Vice President,
First Interstate Bank of Texas

Enclosure

Board of Governors of the Federal Reserve System
OMB Number: 7100-0036
Federal Deposit Insurance Corporation
OMB Number: 3064-0052
Office of the Comptroller of the Currency
OMB Number: 1557-0081
Expires February 28, 1995

Federal Financial Institutions Examination Council

Please refer to page i, Table of Contents, for the required disclosure of estimated burden.

1

Consolidated Reports of Condition and Income for A Bank With Domestic and Foreign Offices—FFIEC 031

Report at the close of business June 30, 1993 (930630)

This report is required by law: 12 U.S.C. §324 (State member banks); 12 U.S.C. §1817 (State nonmember banks); and 12 U.S.C. §161 (National banks).

This report form is to be filed by banks with branches and consolidated subsidiaries in U.S. territories and possessions, Edge or Agreement subsidiaries, foreign branches, consolidated foreign subsidiaries, or International Banking Facilities.

NOTE: The Reports of Condition and Income must be signed by an authorized officer and the Report of Condition must be attested to by not less than two directors (trustees) for State nonmember banks and three directors for State member and National banks.

I, Dennis Steen, Senior Vice President
Name and Title of Officer Authorized to Sign Report

of the named bank do hereby declare that these Reports of Condition and Income (including the supporting schedules) have been prepared in conformance with the instructions issued by the appropriate Federal regulatory authority and are true to the best of my knowledge and belief.

Signature of Officer Authorized to Sign Report

August 2, 1993
Date of Signature

The Reports of Condition and Income are to be prepared in accordance with Federal regulatory authority instructions. NOTE: These instructions may in some cases differ from generally accepted accounting principles.

We, the undersigned directors (trustees), attest to the correctness of this Report of Condition (including the supporting schedules) and declare that it has been examined by us and to the best of our knowledge and belief has been prepared in conformance with the instructions issued by the appropriate Federal regulatory authority and is true and correct.

Director (Trustee) Linnet F. Deily

Director (Trustee) Dr. Peter C. Marzio

Director (Trustee) Jack T. Trotter

For Banks Submitting Hard Copy Report Forms:

State Member Banks: Return the original and one copy to the appropriate Federal Reserve District Bank.

State Nonmember Banks: Return the original only in the *special return address envelope provided*. If express mail is used in lieu of the special return address envelope, return the original only to the FDIC, c/o Quality Data Systems, 2139 Espey Court, Crofton, MD 21114.

National Banks: Return the original only in the *special return address envelope provided*. If express mail is used in lieu of the special return address envelope, return the original only to the FDIC, c/o Quality Data Systems, 2139 Espey Court, Crofton, MD 21114.

FDIC Certificate Number 24344

CALL NO. 184 31 06-30-93
CERT: 24344 00001 STBK 48-3778
FIRST INTERSTATE BANK OF TEXAS, NATI
P.O. BOX 3326
HOUSTON, TX 77253-3326

First Interstate Bank of Texas, NA
P.O. Box 3326
Houston, TX 77253-3326

Call Date: 06/30/93
Vendor ID: D

ST-BK: 48-3778
CERT: 24344

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Transit Number: 11300106

Consolidated Report of Income for the period January 1, 1993 - June 30, 1993

All Report of Income schedules are to be reported on a calendar year-to-date basis in thousands of dollars.

Schedule RI - Income Statement

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	RIAD	Dollar Amounts in Thousands	
1. Interest income:			
a. Interest and fee income on loans:			
(1) In domestic offices:			
(a) Loans secured by real estate	4011	32,850	1.a.1a
(b) Loans to depository institutions	4019	9	1.a.1b
(c) Loans to finance agricultural production and other loans to farmers	4024	52	1.a.1c
(d) Commercial and industrial loans	4012	37,034	1.a.1d
(e) Acceptances of other banks	4026	0	1.a.1e
(f) Loans to individuals for household, family, and other personal expenditures:			
(1) Credit cards and related plans	4054	2,918	1.a.1f1
(2) Other	4055	8,355	1.a.1f2
(g) Loans to foreign governments and official institutions	4056	0	1.a.1g
(h) Obligations (other than securities and leases) of states and political subdivisions in the U.S.:			
(1) Taxable obligations	4503	208	1.a.1h1
(2) Tax-exempt obligations	4504	3,671	1.a.1h2
(i) All other loans in domestic offices	4058	2,245	1.a.1i
(2) In foreign offices, Edge and Agreement subsidiaries, and IBFs	4059	0	1.a.2
b. Income from lease financing receivables:			
(1) Taxable leases	4505	7	1.b.1
(2) Tax-exempt leases	4307	0	1.b.2
c. Interest income on balances due from depository institutions:(1)			
(1) In domestic offices	4105	67	1.c.1
(2) In foreign offices, Edge and Agreement subsidiaries, and IBFs	4106	0	1.c.2
d. Interest and dividend income on securities:			
(1) U.S. Treasury securities and U.S. Government agency and corporation obligations	4027	45,071	1.d.1
(2) Securities issued by states and political subdivisions in the U.S.:			
(a) Taxable securities	4506	42	1.d.2a
(b) Tax-exempt securities	4507	3	1.d.2b
(3) Other domestic debt securities	3657	3,898	1.d.3
(4) Foreign debt securities	3658	112	1.d.4
(5) Equity securities (including investments in mutual funds)	3659	918	1.d.5
e. Interest income from assets held in trading accounts	4069	4	1.e

(1) Includes interest income on time certificates of deposit not held in trading accounts.

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Schedule RI Continued

Dollar Amounts in Thous

	RIAD	Year-to-date		
1. Interest income (continued)				
f. Interest income federal funds sold and securities purchased under agreements to resell in domestic offices of the bank and of its Edge and Agreement subsidiaries, and in IBFs	4020	1,484		1.f
g. Total interest income (sum of items 1.a through 1.f)	4107	138,948		1.g
2. Interest expense:				
a. Interest on deposits:				
(1) Interest on deposits in domestic offices:				
(a) Transaction accounts (NOW accounts, ATS accounts, and telephone and preauthorized transfer accounts)	4508	6,029		2.a.1
(b) Nontransaction accounts:				
(1) Money market deposit accounts (MMDAs)	4509	16,300		2.a.1
(2) Other savings deposits	4511	2,807		2.a.1
(3) Time certificates of deposit of $ 100,000 or more	4174	3,499		2.a.1
(4) All other time deposits	4512	14,553		2.a.1
(2) Interest on deposits in foreign offices, Edge and Agreement subsidiaries, and IBFs	4172	0		2.a.2
b. Expense of federal funds purchased and securities sold under agreements to repurchase in domestic offices of the bank and of its Edge and Agreement subsidiaries, and in IBFs	4180	846		2.b
c. Interest on demand notes issued to the U.S. Treasury and on other borrowed money	4185	232		2.c
d. Interest on mortgage indebtedness and obligations under capitalized leases	4072	175		2.d
e. Interest on subordinated notes and debentures	4200	0		2.e
f. Total interest expense (sum of items 2.a through 2.e)	4073	44,441		2.f
3. Net interest income (item 1.g minus 2.f)	4074		94,507	3.
4. Provisions:				
a. Provision for loan and lease losses	4230		3,600	4.a
b. Provision for allocated transfer risk	4243		0	4.b
5. Noninterest income:				
a. Income from fiduciary activities	4070	4,394		5.a
b. Service charges on deposit accounts in domestic offices	4080	40,868		5.b
c. Trading gains (losses) and fees from foreign exchange transactions	4075	356		5.c
d. Other foreign transaction gains (losses)	4076	0		5.d
e. Gains (losses) and fees from assets held in trading accounts	4077	2,572		5.e
f. Other noninterest income:				
(1) Other fee income	5407	7,404		5.f.1
(2) All other noninterest income *	5408	2,781		5.f.2
g. Total noninterest income (sum of items 5.a through 5.f)	4079		58,375	5.g
6. Gains (losses) on securities not held in trading accounts	4091		140	6.
7. Noninterest expense:				
a. Salaries and employee benefits	4135	48,643		7.a
b. Expenses of premises and fixed assets (net of rental income) (excluding salaries and employee benefits and mortgage interest)	4217	17,782		7.b
c. Other noninterest expense *	4092	36,269		7.c
d. Total noninterest expense (sum of items 7.a through 7.c)	4093		102,694	7.d
8. Income (loss) before income taxes and extraordinary items and other adjustments (item 3 plus or minus items 4.a, 4.b, 5.g, 6, and 7.d)	4301		46,728	8.
9. Applicable income taxes (on item 8)	4302		8,341	9.
10. Income (loss) before extraordinary items and other adjustments (item 8 minus 9)	4300		38,387	10.

* Describe on Schedule RI-E - Explanations.

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P.O. Box 3326
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Schedule RI - Continued

	RIAD	Year-to-date	Dollar Amounts in Thousands	
11. Extraordinary items and other adjustments:				
a. Extraordinary items and other adjustments, gross of income taxes	4310	30,635		11.a
b. Applicable income (on item 11.a)	4315	(1,085)		11.b
c. Extraordinary items and other adjustments, net of income taxes (item 11.a minus 11.b)	4320		31,720	11.c
12. Net income (loss) (sum of items 10 and 11.c)	4340		70,107	12.

Memoranda

	RIAD	Dollar Amounts in Thousands Year-to-date	
1. Interest expense incurred to carry tax-exempt securities, loans, and leases acquired after August 1986, that is not deductible for federal income tax purposes	4513	416	M.1
2. Not applicable			
3. Estimated foreign tax credit included in applicable income taxes, items 9 and 11.b above	4309	0	M.3
4. To be completed only by banks with $1 billion or more in total assets: Taxable equivalent adjustment to "Income loss) before income taxes and extraordinary items and other adjustments" (item above)	1244	1,666	M.4
5. Number of full-time equivalent employees payrol at end of current period (round to nearest whole number)	4150	Number 2,810	M.5

Schedule RI-A - Changes in Equity Capital

Indicate decreases and losses in parentheses.

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	RIAD	Dollar Amounts in Thousands	
1. Total equity capital originally reported in the December 31 1992, Reports of Condition and Income	3215	462,838	1.
2. Equity capital adjustments from amended Reports of Income, net *	3216	0	2.
3. Amended balance end of previous calendar year (sum of items 1 and 2)	3217	462,838	3.
4. Net income (loss) (must equal Schedule RI, item 12)	4340	70,107	4.
5. Sale, conversion, acquisition, or retirement of capital stock, net	4346	0	5.
6. Changes incident to business combinations, net	4356	11,170	6.
7. LESS: Cash dividends declared on preferred stock	4470	0	7.
8. LESS: Cash dividends declared on common stock	4460	0	8.
9. Cumulative effect of changes in accounting principles from prior years * (see instructions for this schedule)	4411	0	9.
10. Corrections of material accounting errors from prior years * (see instructions for this schedule)	4412	0	10.
11. Change in net unrealized loss on marketable equity securities	4413	0	11.
12. Foreign currency translation adjustments	4414	0	12.
13. Other transactions with parent holding company * (not included in items 5, 7, or above)	4415	(22,248)	13.
14. Total equity capital end of current period (sum of items 3 through 13) (must equal Schedule RC, item 28)	3210	521,867	14.

* Describe on Schedule RI-E - Explanations.

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Schedule RI-B - Charge-offs and Recoveries and Changes in Allowance for Loan and Lease Losses

Part I. Charge-offs and Recoveries on Loans and Leases

Part I excludes charge-offs and recoveries through the allocated transfer risk reserve.

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Dollar Amounts in Thousands

	calendar year-to-date				
	(Column A) Charge-offs		(Column B) Recoveries		
1. Loans secured by real estate:	RIAD		RIAD		
a. To U.S. addressees (domicile)	4651. .	1,861	4661. .	1,840	1.a
b. To non-U.S. addressees (domicile)	4652. .	0	4662. .	0	1.b
2. Loans to depository institutions and acceptances of other banks:					
a. To U.S. banks and other U.S. depository institutions	4653. .	0	4663. .	0	2.a
b. To foreign banks	4654. .	0	4664. .	0	2.b
3. Loans to finance agricultural production and other loans to farmers	4655. .	0	4665. .	0	3.
4. Commercial and industrial loans:					
a. To U.S. addressees (domicile)	4645. .	3,187	4617. .	1,912	4.a
b. To non-U.S. addressees (domicile)	4646. .	0	4618. .	0	4.b
5. Loans to individuals for household, family, and other personal expenditures:					
a. Credit cards and related plans	4656. .	313	4666. .	46	5.a
b. Other (includes single payment, installment, and all student loans)	4657. .	465	4667. .	406	5.b
6. Loans to foreign governments and official institutions	4643. .	0	4627. .	0	6.
7. All other loans	4644. .	330	4628. .	80	7.
8. Lease financing receivables:					
a. Of U.S. addressees (domicile)	4658. .	0	4668. .	46	8.a
b. Of non-U.S. addressees (domicile)	4659. .	0	4669. .	0	8.b
9. Total (sum of items 1 through 8)	4635. .	6,156	4605. .	4,330	9.

Memoranda

Dollar Amounts in Thousands

	Cumulative Charge-offs Jan 1 1986 through Dec 31 1989		Cumulative Recoveries Jan 1 1986 through Report Date		
To be completed by national banks only.					
1. Charge-offs and recoveries of Special-Category Loans, as defined for this Call Report by the Comptroller of the Currency	RIAD		RIAD 4784. .	1,441	M.1

	calendar year-to-date				
Memorandum items 2 and 3 are to be completed by all banks.	(Column A) Charge-offs		(Column B) Recoveries		
2. Loans to finance commercial real estate, construction, and land development activities (not secured by real estate) included in Schedule RI-B, part I, items 4 and 7, above	RIAD 5409. .	0	RIAD 5410. .	0	M.2
3. Loans secured by real estate in domestic offices (included in Schedule RI-B, part I, item 1, above):					
a. Construction and land development	3582. .	679	3583. .	642	M.3.a
b. Secured by farmland	3584. .	0	3585. .	0	M.3.b
c. Secured by 1-4 family residential properties:					
(1) Revolving, open-end loans secured by 1-4 family residential properties and extended under lines of credit	5411. .	0	5412. .	0	M.3.c1
(2) All other loans secured by 1-4 family residential properties	5413. .	436	5414. .	104	M.3.c2
d. Secured by multifamily (5 or more) residential properties	3588. .	60	3589. .	0	M.3.d
e. Secured by nonfarm nonresidential properties	3590. .	686	3591. .	1,094	M.3.e

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Schedule RI-B - Continued

Part II. Changes in Allowance for Loan and Lease Losses and in Allocated Transfer Risk Reserve

		(Column A) Allowance for Loan and Lease Losses		(Column B) Allocated Transfer Risk Reserve	
	RIAD	Dollar Amounts in Thousands	RIAD		
1. Balance originally reported in the December 31, 1992, Reports of Condition and Income	3124. .	74,304	3131. .	0	1.
2. Recoveries (column A must equal part I, item 9, column B above)	4605. .	4,330	3132. .	0	2.
3. LESS: Charge-offs (column A must equal part I, item 9, column A above)	4635. .	6,156	3133. .	0	3.
4. Provision (column A must equal Schedule RI, item 4.a; column B must equal schedule RI, item 4.b)	4230. .	3,600	4243. .	0	4.
5. Adjustments * (see instructions for this schedule)	4815. .	506	3134. .	0	5.
6. Balance end of current period (sum of items 1 through 5) (column A must equal Schedule RC, item 4.b; column B must equal Schedule RC, item 4.c)	3123. .	76,584	3128. .	0	6.

* Describe on Schedule RI-E - Explanations.

Schedule RI-C - Applicable Income Taxes by Taxing Authority

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Schedule RI-C is to be reported with the December Report of Income.

	RIAD	Dollar Amounts in Thousands	
1. Federal	4780. .	N/A	1.
2. State and local	4790. .	N/A	2.
3. Foreign	4795. .	N/A	3.
4. Total (sum of items 1 through 3) (must equal sum of Schedule RI, items 9 and 11.b)	4770. .	N/A	4.
5. Deferred portion of item 4 — RIAD 4772. . N/A		. . . . . .	5.

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Schedule RI-D - Income from International Operations

For all banks with foreign offices, Edge or Agreement subsidiaries, or IBFs where international operations account for more than 10 percent of total revenues, total assets, or net income.

Part I. Estimated Income from International Operations

I492 <-

	RIAD	Dollar Amounts in Thousands Year-to-date	
1. Interest income and expense booked at foreign offices, Edge and Agreement subsidiaries, and IBFs:			
a. Interest income booked	4837	N/A	1.a
b. Interest expense booked	4838	N/A	1.b
c. Net interest income booked at foreign offices, Edge and Agreement subsidiaries, and IBFs (item 1.a minus 1.b)	4839	N/A	1.c
2. Adjustments for booking location of international operations:			
a. Net interest income attributable to international operations booked at domestic offices	4840	N/A	2.a
b. Net interest income attributable to domestic business booked at foreign offices	4841	N/A	2.b
c. Net booking location adjustment (item 2.a minus 2.b)	4842	N/A	2.c
3. Noninterest income and expense attributable to international operations:			
a. Noninterest income attributable to international operations	4097	N/A	3.a
b. Provision for loan and lease losses attributable to international operations	4235	N/A	3.b
c. Other noninterest expense attributable to international operations	4239	N/A	3.c
d. Net noninterest income (expense) attributable to international operations (item 3.a minus 3.b and 3.c)	4843	N/A	3.d
4. Estimated pretax income attributable to international operations before capital allocation adjustment (sum of items 1.c, 2.c, and 3.d)	4844	N/A	4.
5. Adjustment to pretax income for internal allocations to international operations to reflect the effects of equity capital on overall bank funding costs	4845	N/A	5.
6. Estimated pretax income attributable to international operations after capital allocation adjustment (sum of items 4 and 5)	4846	N/A	6.
7. Income taxes attributable to income from international operations as estimated in item 6	4797	N/A	7.
8. Estimated net income attributable to international operations (item 6 minus 7)	4341	N/A	8.

Memoranda

		Dollar Amounts in Thousands	
1. Intracompany interest income included in item 1.a above	4847	N/A	M.1
2. Intracompany interest expense included in item 1.b above	4848	N/A	M.2

Part II. Supplementary Details on Income from International Operations Required by the Departments of Commerce and Treasury for Purposes of the U.S. International Accounts and the U.S. National Income and Product Accounts

	RIAD	Dollar Amounts in Thousands Year-to-date	
1. Interest income booked at IBFs	4849	N/A	1.
2. Interest expense booked at IBFs	4850	N/A	2.
3. Noninterest income attributable to international operations booked at domestic offices (excluding IBFs):			
a. Gains (losses) and extraordinary items	5491	N/A	3.a
b. Fees and other noninterest income	5492	N/A	3.b
4. Provision for loan and lease losses attributable to international operations booked at domestic offices (excluding IBFs)	4852	N/A	4.
5. Other noninterest expense attributable to international operations booked at domestic offices (excluding IBFs)	4853	N/A	5.

Schedule RI-E - Explanations

Schedule RI-E is to be completed each quarter on a calendar year-to-date basis.

Detail all adjustments in Schedules RI-A and RI-B, all extraordinary items and other adjustments in Schedule RI, and all significant items of other noninterest income and other noninterest expense in Schedule RI. (See instructions for details.)

I495 <-

	RIAD	Dollar Amounts in Thousands / Year-to-date	
1. All other noninterest income (from Schedule RI, item 5.f.(2))			
Report amounts that exceed 10% of Schedule RI, item 5.f.(2):			
a. Net gains on other real estate owned	5415	N/A	1.a
b. Net gains on sales of loans	5416	N/A	1.b
c. Net gains on sales of premises and fixed assets	5417	N/A	1.c
Itemize and describe the three largest other amounts that exceed 10% of Schedule RI, item 5.f.(2):			
TEXT			
d. 4461: Customer Supply Fees	4461	605	1.d
e. 4462: Net Operating Loss on Unconsolidated Sub	4462	(300)	1.e
f. 4463:	4463	N/A	1.f
2. Other noninterest expense (from Schedule RI, item 7.c):			
a. Amortization expense of intangible assets	4531	227	2.a
Report amounts that exceed 10% of Schedule RI, item 7.c:			
b. Net losses on other real estate owned	5418	N/A	2.b
c. Net losses on sales of loans	5419	N/A	2.c
d. Net losses on sales of premises and fixed assets	5420	N/A	2.d
Itemize and describe the three largest other amounts that exceed 10% of Schedule RI, item 7.c:			
TEXT			
e. 4464: Data Processing Expense	4464	4,789	2.e
f. 4467: FDIC Assessment Expense	4467	5,424	2.f
g. 4468:	4468	N/A	2.g
3. Extraordinary items and other adjustments (from Schedule RI, item 11.a) and applicable income tax effect (from Schedule RI, item 11.b) (itemize and describe all extraordinary items and other adjustments):			
TEXT			
a. (1) 4469: Adoption of FAS 106	4469	(2,947)	3.a.1
(2) Applicable income tax effect — RIAD 4486 (1,085)			3.a.2
b. (1) 4487: Adoption of FAS 109	4487	33,582	3.b.1
(2) Applicable income tax effect — RIAD 4488 0			3.b.2
c. (1) 4489:	4489	0	3.c.1
(2) Applicable income tax effect — RIAD 4491 0			3.c.2
4. Equity capital adjustments from amended Reports of Income (from Schedule RI-A, item 2) (itemize and describe all adjustments):			
TEXT			
a. 4492:	4492	N/A	4.a
b. 4493:	4493	N/A	4.b
5. Cumulative effect of changes in accounting principles from prior years (from Schedule RI-A, item 9) (itemize and describe all changes in accounting principles):			
TEXT			
a. 4494:	4494	N/A	5.a
b. 4495:	4495	N/A	5.b
6. Corrections of material accounting errors from prior years (from Schedule RI-A, item 10) (itemize and describe all corrections):			
TEXT			
a. 4496:	4496	N/A	6.a
b. 4497:	4497	N/A	6.b

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Schedule RI-E - Continued

Dollar Amounts in Thousands

7. Other transactions with parent holding company (from Schedule RI-A, item 13) (itemize and describe all such transactions):

TEXT		RIAD	Year-to-date	
a. 4498:	Return of Surplus to Holding Company	4498. .	(22,248)	7.a
b. 4499:		4499. .	N/A	7.b

8. Adjustments to allowance for loan and lease losses (from Schedule RI-B, part II, item 5) (itemize and describe all adjustments):

TEXT				
a. 4521:	Branch Sale and Loan Sale	4521. .	(191)	8.a
b. 4522:	Merge FI Jacksonville Allow for Loan Loss	4522. .	697	8.b

I498 I499 <-

9. Other explanations (the space below is provided for the bank to briefly describe, at its option, any other significant items affecting the Report of Income):

No comment: X (RIAD 4769)

Other explanations (please type or print clearly):
(TEXT 4769)

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Consolidated Report of Condition for Insured Commercial and State-Chartered Savings Banks for June 30, 1993

All schedules are to be reported in thousands of dollars. Unless otherwise indicated, report the amount outstanding as of the last business day of the quarter.

Schedule RC - Balance Sheet

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	RCFD		RCFD	Dollar Amounts in Thousands	
ASSETS					
1. Cash and balances due from depository institutions (from Schedule RC-A):					
a. Noninterest-bearing balances and currency and coin (1)			0081	638,845	1.a
b. Interest-bearing balances (2)			0071	49,030	1.b
2. Securities (from Schedule RC-B)			0390	1,604,472	2.
3. Federal funds sold and securities purchased under agreements to resell in domestic offices of the bank and of its Edge and Agreement subsidiaries, and in IBFs:					
a. Federal funds sold			0276	156,000	3.a
b. Securities purchased under agreements to resell			0277	0	3.b
4. Loans and lease financing receivables:					
a. Loans and leases, net of unearned income (from Schedule RC-C)	2122	2,723,707			4.a
b. LESS: Allowance for loan and lease losses	3123	76,584			4.b
c. LESS: Allocated transfer risk reserve	3128	0			4.c
d. Loans and leases, net of unearned income, allowance, and reserve (item 4.a minus 4.b and 4.c)			2125	2,647,123	4.d
5. Assets held in trading accounts			2146	6,495	5.
6. Premises and fixed assets (including capitalized leases)			2145	104,680	6.
7. Other real estate owned (from Schedule RC-M)			2150	29,196	7.
8. Investments in unconsolidated subsidiaries and associated companies (from Schedule RC-M)			2130	22,019	8.
9. Customers' liability to this bank on acceptances outstanding			2155	11,852	9.
10. Intangible assets (from Schedule RC-M)			2143	1,399	10.
11. Other assets (from Schedule RC-F)			2160	93,479	11.
12. Total assets (sum of items 1 through 11)			2170	5,364,590	12.

(1) Includes cash items in process of collection and unposted debits.
(2) Includes time certificates of deposit not held in trading accounts.

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Schedule RC - Continued

Dollar Amounts in Thousands

LIABILITIES				
13. Deposits:				
a. In domestic offices (sum of totals of columns A and C from Schedule RC-E, Part I)	RCON 2200		4,669,739	13.a
(1) Noninterest-bearing (1)	6631	1,470,701		13.a.1
(2) Interest-bearing	6636	3,199,038		13.a.2
b. In foreign offices, Edge and Agreement subsidiaries, and IBFs (from Schedule RC-E, part II)	RCFN 2200		0	13.b
(1) Noninterest-bearing	6631	0		13.b.1
(2) Interest-bearing	6636	0		13.b.2
14. Federal funds purchased and securities sold under agreements to repurchase in domestic offices of the bank and of its Edge and Agreement subsidiaries and in IBFs:	RCFD			
a. Federal funds purchased	0278		50,750	14.a
b. Securities sold under agreements to repurchase	0279		47,171	14.b
15. Demand notes issued to the U.S. Treasury	RCON 2840		0	15.
16. Other borrowed money	RCFD 2850		1,085	16.
17. Mortgage indebtedness and obligations under capitalized leases	2910		2,279	17.
18. Bank's liability on acceptances executed and outstanding	2920		11,852	18.
19. Subordinated and debentures	3200		0	19.
20. Other liabilities (from Schedule RC-G)	2930		59,847	20.
21. Total liabilities (sum of tems 13 through 20)	2948		4,842,723	21.
22. Limited-life preferred stock and related surplus	3282		0	22.
EQUITY CAPITAL				
23. Perpetual preferred stock and related surplus	3838		0	23.
24. Common stock	3230		50,000	24.
25. Surplus (exclude all surplus related to preferred stock)	3839		952,014	25.
26. a. Undivided profits and capital reserves	3632		(480,147)	26.a
b. LESS: Net unrealized loss on marketable equity securities	0297		0	26.b
27. Cumulative foreign currency translation adjustments	3284		0	27.
28. Total equity capital (sum of items 23 through 27)	3210		521,867	28.
29. Total liabi ities, imited-life preferred stock, and equity capital (sum of items 21, 22, and 28)	3300		5,364,590	29.

Memorandum

To be reported only with the March Report of Condition.

1. Indicate in the box at the right the number of the statement below that best describes the most comprehensive level of auditing work performed for the bank by independent external auditors as of any date during 1992	RCFD 6724	NUMBER N/A		M.1

1 = Independent audit of the bank conducted in accordance with generally accepted auditing standards by a certified public accounting firm which submits a report on the bank
2 = Independent audit of the bank's parent holding company conducted in accordance with generally accepted auditing standards by a certified public accounting firm which submits a report on the consolidated holding company (but not on the bank separately)
3 = Directors' examination of the bank conducted in accordance with generally accepted auditing standards by a certified public accounting firm (may be required by state chartering authority)
4 = Directors' examination of the bank performed by other external auditors (may be required by state chartering authority)
5 = Review of the bank's financial statements by external auditors
6 = Compilation of the bank's financial statements by external auditors
7 = Other audit procedures (excluding tax preparation work)
8 = No external audit work

(1) Includes total demand deposits and noninterest-bearing time and savings deposits

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le RC-A - Cash and Balances Due From Depository Institutions

sets held in trading accounts.

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Dollar Amounts in Thousands		(Column A) Consolidated Bank		(Column B) Domestic Offices	
	RCFD		RCON		
ms in process of collection, unposted and currency and coin	0022. .	528,769		. . . .	1.
items in process of collection and unposted ts		. . . .	0020. .	430,009	1.a
ncy and coin		. . . .	0080. .	98,760	1.b
due from depository institutions in the U.S.		. . . .	0082. .	78,369	2.
branches and agencies of foreign banks uding their IBFs)	0083. .	0		. . . .	2.a
commercial banks in the U.S. and other sitory institutions in the U.S. (including IBFs)	0085. .	78,369		. . . .	2.b
due from banks in foreign countries and central banks		. . . .	0070. .	49,986	3.
gn branches of other U.S. banks	0073. .	0		. . . .	3.a
banks in foreign countries and foreign al banks	0074. .	49,986		. . . .	3.b
due from Federal Reserve Banks	0090. .	30,751	0090. .	30,751	4.
um of items 1 through 4) (total of column A al Schedule RC, item 1)	0010. .	687,875	0010. .	687,875	5.

ndum

Dollar Amounts in Thousands			
est-bearing balances due from commercial banks in the U.S. d in item 2, column B above)	RCON 0050. .	78,339	M.1

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Schedule RC-B - Securities

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Exclude assets held in trading accounts.

Dollar Amounts in Thousands

	Consolidated Bank				Domestic Offices		
		(Column A) Book Value		(Column B) Market Value (1)		(Column C) Book Value	
	RCFD		RCFD		RCON		
1. U.S. Treasury securities	0400..	641,653	0401..	653,417	0400..	641,653	1.
2. U.S. Government agency and corporation obligations:							
a. All holdings of U.S. Government-issued or -guaranteed certificates of participation in pools of residential mortgages:							
(1) Issued by FNMA and FHLMC	3760..	244,689	3761..	249,717	3760..	244,689	2.a1
(2) Guaranteed by GNMA (exclude FNMA and FHLMC issues)	3762..	114,546	3763..	120,674	3762..	114,546	2.a2
b. All other	0604..	432,227	0605..	434,298		....	2.b
(1) Collateralized mortgage obligations issued by FNMA and FHLMC (include REMICs)		....		....	3764..	410,301	2.b1
(2) All other U.S. Government-sponsored agency obligations (2)		....		....	3765..	21,926	2.b2
(3) All other U.S. Government agency obligations (3)		....		....	3766..	0	2.b3
3. Securities issued by states and political subdivisions in the U.S.	0402..	878	0403..	1,065		....	3.
a. General obligations		....		....	3767..	808	3.a
b. Revenue obligations		....		....	3768..	70	3.b
c. Industrial development and similar obligations		....		....	3769..	0	3.c
4. Other domestic debt securities:							
a. All holdings of private (i.e., non-government-issued or -guaranteed) certificates of participation in pools of residential mortgages	0408..	0	0409..	0	0408..	0	4.a
b. All other domestic debt securities:							
(1) Privately-issued collateralized mortgage obligations (include REMICs)	5361..	33,142	5362..	32,907	5361..	33,142	4.b1
(2) All other	5363..	102,737	5364..	103,892	5363..	102,737	4.b2
5. Foreign debt securities	3635..	4,030	3636..	4,030	3635..	4,030	5.
6. Equity securities:							
a. Marketable equity securities:							
(1) Investments in mutual funds	3637..	0	3638..	0	3637..	0	6.a1
(2) Other marketable equity securities	3639..	171	3640..	171	3639..	171	6.a2
(3) LESS: Net unrealized loss on marketable equity securities	3641..	0		....	3641..	0	6.a3
b. Other equity securities (includes Federal Reserve stock)	3642..	30,399	3643..	30,399	3642..	30,399	6.b
7. Total (sum of items 1 through 6) (total of column A must equal Schedule RC, item 2)	0390..	1,604,472	0391..	1,630,570	0390..	1,604,472	7.

(1) See discussion in Glossary entry for "market value of securities."
(2) Includes obligations (other than certificates of participation in pools of residential mortgages, CMOs, and REMICs) issued by the Farm Credit System, the Federal Home Loan Bank System, the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association, the Financing Corporation, Resolution Funding Corporation, the Student Loan Marketing Association, and the Tennessee Valley Authority.
(3) Includes Small Business Administration "Guaranteed Loan Pool Certificates," U.S. Maritime Administration obligations, and Export-Import Bank participation certificates.

Schedule RC-B - Continued

Memoranda

	RCFD	Dollar Amounts in Thousands --- Consolidated Bank --- Book Value	
1. Pledged securities	0416	260,693	M.1
2. Maturity and repricing data for debt securities (1,2) (excluding those in nonaccrual status):			
a. Fixed rate debt securities with a remaining maturity of:			
(1) Three months or less	0343	40,258	M.2.a1
(2) Over three months through 12 months	0344	151,612	M.2.a2
(3) Over one year through five years	0345	583,326	M.2.a3
(4) Over five years	0346	553,286	M.2.a4
(5) Total fixed rate debt securities (sum of Memorandum items 2.a.(1) through 2.a.(4))	0347	1,328,482	M.2.a5
b. Floating rate debt securities with a repricing frequency of:			
(1) Quarterly or more frequently	4544	204,295	M.2.b1
(2) Annually or more frequently, but less frequently than quarterly	4545	41,125	M.2.b2
(3) Every five years or more frequently, but less frequently than annually	4551	0	M.2.b3
(4) Less frequently than every 5 years	4552	0	M.2.b4
(5) Total floating rate debt securities (sum of Memorandum items 2.b.(1) through 2.b.(4))	4553	245,420	M.2.b5
c. Total debt securities (sum of Memorandum items 2.a.(5) and 2.b.(5)) (must equal total debt securities from Schedule RC-B, sum of items 1 through 5, column A, minus nonaccrual debt securities included in Schedule RC-N, item 9, column C)	0393	1,573,902	M.2.c
3. Taxable securites issued by states and political subdivisions in the U.S. (included in Schedule RC-B, item 3, column A, above)	0301	800	M.3
4. Debt securities restructured and in compliance with modified terms (included in Schedule RC-B, items 3 through 5, column A, above)	5365	0	M.4
5. Debt securities held for sale (included in Schedule RC-B, items 1 through 5, column A, above)	5366	0	M.5
6. Floating rate debt securities with a remaining maturity of one year or less (included in Memorandum item 2.b.(5) above)	5519	1,035	M.6

(1) Exclude equity securities, e.g., investments in mutual funds, Federal Reserve stock, common stock, and preferred stock.
(2) Memorandum item 2 is not applicable to savings banks that must complete supplemental Schedule RC-J.

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Schedule RC-C - Loans and Lease Financing Receivables

Part I. Loans and Leases

Do not deduct the allowance for loan and lease losses from amounts reported in this schedule. Report total loans and leases, net of unearned income. Exclude assets held in trading accounts.

C415 <-

Dollar Amounts in Thousands

	RCFD	(Column A) Consolidated Bank	RCON	(Column B) Domestic Offices	
1. Loans secured by real estate	1410	869,244			1.
a. Construction and land development			1415	100,767	1.a
b. Secured by farmland (including farm residential and other improvements)			1420	6,988	1.b
c. Secured by 1-4 family residential properties:					
(1) Revolving, open-end loans secured by 1-4 family residential properties and extended under lines of credit			1797	0	1.c1
(2) All other loans secured by 1-4 family residential properties:					
(a) Secured by first liens			5367	252,779	1.c2a
(b) Secured by junior liens			5368	37,148	1.c2b
d. Secured by multifamily (5 or more) residential properties			1460	42,416	1.d
e. Secured by nonfarm nonresidential properties			1480	429,146	1.e
2. Loans to depository institutions:					
a. To commercial banks in the U.S.			1505	1,458	2.a
(1) To U.S. branches and agencies of foreign banks	1506	0			2.a1
(2) To other commercial banks in the U.S.	1507	1,458			2.a2
b. To other depository institutions in the U.S.	1517	2,000	1517	2,000	2.b
c. To banks in foreign countries			1510	7,865	2.c
(1) To foreign branches of other U.S. banks	1513	0			2.c1
(2) To other banks in foreign countries	1516	7,865			2.c2
3. Loans to finance agricultural production and other loans to farmers	1590	3,089	1590	3,089	3.
4. Commercial and industrial loans:					
To U.S. addressees (domicile)	1763	1,259,691	1763	1,259,691	4.a
b. To non-U.S. addressees (domicile)	1764	6,819	1764	6,819	4.b
5. Acceptances of other banks:					
a. Of U.S. banks	1756	0	1756	0	5.a
b. Of foreign banks	1757	0	1757	0	5.b
6. Loans to individuals for household, family, and other personal expenditures (i.e., consumer loans) (includes purchased paper)			1975	268,113	6.
a. Credit cards and related plans (includes check credit and other revolving credit plans)	2008	66,550			6.a
b. Other (includes single payment, installment, and all student loans)	2011	201,563			6.b
7. Loans to foreign governments and official institutions (including foreign central banks)	2081	0	2081	0	7.
8. Obligations (other than securities and leases) of states and political subdivisions in the U.S. (includes nonrated industrial development obligations):					
a. Taxable obligations	2033	5,480	2033	5,480	8.a
b. Tax-exempt obligations	2079	85,469	2079	85,469	8.b
9. Other loans	1563	208,967			9.
a. Loans for purchasing or carrying securities (secured and unsecured)			1545	56,428	9.a
b. All other loans (exclude consumer loans)			1564	152,539	9.b
10. Lease financing receivables (net of unearned income)			2165	5,512	10.
a. Of U.S. addressees (domicile)	2182	5,512			10.a
b. Of non-U.S. addressees (domicile)	2183	0			10.b
11. LESS: Any unearned income on loans reflected in items 1-9 above	2123	0	2123	0	11.
12. Total loans and leases, net of unearned income (sum of items 1 through 10 minus item 11) (total of column A must equal Schedule RC, item 4.a)	2122	2,723,707	2122	2,723,707	12.

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Schedule RC-C - Continued

Part I. Continued

Memoranda

Dollar Amounts in Thousands

	RCFD	(Column A) Consolidated Bank	RCON	(Column B) Domestic Offices	
1. Commercial paper included in Schedule RC-C, part I, above	1496	0	1496	0	M.1
2. Loans and leases restructured and in compliance with modified (included in Schedule RC-C, part I, above):					
a. Loans secured by real estate:					
(1) To U.S. addressees (domicile)	1687	0			M.2.a1
(2) To non-U.S. addressees (domicile)	1689	0			M.2.a2
b. Loans to finance agricultural production and other loans to farmers	1613	0			M.2.b
c. Commercial and industrial loans:					
(1) To U.S. addressees (domicile)	1758	0			M.2.c1
(2) To non-U.S. addressees (domicile)	1759	0			M.2.c2
d. All other loans (exclude loans to individuals for household, family, and other personal expenditures)	1615	0			M.2.d
e. Lease financing receivables:					
(1) Of U.S. addressees (domicile)	1789	0			M.2.e1
(2) Of non-U.S. addressees (domicile)	1790	0			M.2.e2
f. Total (sum of Memorandum items 2.a through 2.e)	1616	0			M.2.f
3. Maturity and repricing data for loans and leases (1) (excluding those in nonaccrual status):					
a. Fixed rate loans and leases with a remaining maturity of:					
(1) Three months or less	0348	61,930			M.3.a1
(2) Over three months through 12 months	0349	115,468			M.3.a2
(3) Over one year through five years	0356	521,887			M.3.a3
(4) Over five years	0357	179,583			M.3.a4
(5) Total fixed rate loans and leases (sum of Memorandum items 3.a.(1) through 3.a.(4))	0358	878,868			M.3.a5
b. Floating rate loans with a repricing frequency of:					
(1) Quarterly or more frequently	4554	1,759,119			M.3.b1
(2) Annually or more frequently, but less frequently than quarterly	4555	66,006			M.3.b2
(3) Every five years or more frequently, but less frequently than annually	4561	0			M.3.b3
(4) Less frequently than every five years	4564	0			M.3.b4
(5) Total floating rate loans (sum of Memorandum items 3.b.(1) through 3.b.(4))	4567	1,825,125			M.3.b5
c. Total loans and leases (sum of Memorandum items 3.a.(5) and 3.b.(5)) (must equal the sum of total loans and leases, net, from Schedule RC-C, part I, item 12, plus unearned income from Schedule RC-C, part I, item 11, minus total nonaccrual loans and leases from Schedule RC-N, of items through 8, column C)	1479	2,703,993			M.3.c
4. Loans to finance commercial real estate, construction, and land development activities (not secured by real estate) included in Schedule RC-C, part I, items 4 and 9, column A, page RC-6 (2)	2746	58,862			M.4
5. Loans and leases held for sale (included in Schedule RC-C, part , above)	5369	22,813			M.5
6. Adjustable rate closed-end loans secured by first liens on 1-4 family residential properties (included in Schedule RC-C, part I, item 1.c.(2)(a), column B, page RC-6)			5370	14,300	M.6

(1) Memorandum item is not applicable to savings banks that must complete supplemental Schedule RC-J.
(2) Exclude loans secured by real estate that are included in Schedule RC-C, part I, item 1, column A.

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Schedule RC-C - Continued

Part II. Loans to Small Businesses and Small Farms

Schedule RC-C, Part II is to be reported only with the June Report of Condition.

Report the number and amount currently outstanding as of June 30 of business loans with "original amounts" of $ 1,000,000 or less and farm loans with "original amounts" of $ 500,000 or less. The following guidelines should be used to determine the "original amount" of a loan: (1) For loans drawn down under lines of credit or loan commitments, the "original amount" of the loan is the size of the line of credit or loan commitment when the line of credit or loan commitment was granted. (2) For loan participations and syndications, the "original amount" of the loan participation or syndication is the entire amount of credit originated by the lead lender. (3) For all other loans, the "original amount" is the total amount of the loan at origination.

Loans to Small Businesses

C418 <-

		YES	NO	
1. Indicate in the appropriate box at the right whether all or substantially all of the bank's "Loans secured by nonfarm nonresidential properties" in domestic offices reported in Schedule RC-C, part I, item 1.e, column B, and "Commercial and industrial loans to U.S. addressees" in domestic offices reported in Schedule RC-C, part I, item 4.a, column B, have original amounts of $ 100,000 or less	RCON 6999. .		X	1.

If YES, complete items 2.a and 2.b below, skip items 3 and 4, and go to item 5.
If NO, skip items 2.a and 2.b, complete items 3 and 4 below, and go to item 5.

2. Report the total number of loans currently outstanding for each of the following Schedule RC-C, part I, loan categories:		Number of Loans	
a. "Loans secured by nonfarm nonresidential properties" in domestic offices reported in Schedule RC-C, part I, item 1.e, column B	RCON 5562. .	N/A	2.a
b. "Commercial and industrial loans to U.S. addressees" in domestic offices reported in Schedule RC-C, part I, item 4.a, column B	5563. .	N/A	2.b

Dollar Amounts in Thousands

		(Column A) Number of Loans		(Column B) Amount Currently Outstanding	
3. Number and amount currently outstanding of "Loans secured by nonfarm nonresidential properties" in domestic offices reported in Schedule RC-C, part I, item 1.e, column B (sum of items 3.a through 3.c must be less than or equal to Schedule RC-C, part I, item 1.e, column B):	RCON		RCON		
a. With original amounts of $ 100,000 or less	5564. .	792	5565. .	29,009	3.a
b. With original amounts of more than $ 100,000 through $ 250,000	5566. .	334	5567. .	45,613	3.b
c. With original amounts of more than $ 250,000 through $ 1,000,000	5568. .	224	5569. .	95,617	3.c
4. Number and amount currently outstanding of "Commercial and industrial loans to U.S. addressees" in domestic offices reported in Schedule RC-C, part I, item 4.a, column B (sum of items 4.a through 4.c must be less than or equal to Schedule RC-C, part I, item 4.a, column B):	RCON		RCON		
a. With original amounts of $ 100,000 or less	5570. .	2,625	5571. .	50,761	4.a
b. With original amounts of more than $ 100,000 through $ 250,000	5572. .	279	5573. .	32,194	4.b
c. With original amounts of more than $ 250,000 through $ 1,000,000	5574. .	266	5575. .	98,449	4.c

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Schedule RC-C - Continued

Part II. Continued

Agricultural Loans to Small Farms

5. Indicate in the appropriate box at the right whether all or substantially all of the bank's "Loans secured by farmland (including farm residential and other improvements)" in domestic offices reported in Schedule RC-C, part I, item 1.b, column B, and "Loans to finance agricultural production and other loans to farmers" in domestic offices reported in Schedule RC-C, part I, item 3, column B, have original amounts of $100,000 or less

	RCON	YES	NO	
have original amounts of 100,000 less	6860. .		X	5.

If YES, complete items 6.a and 6.b below and do not complete items 7 and 8.
If NO, skip items 6.a and 6.b and complete items 7 and 8 below.

6. Report the total number of loans currently outstanding for each of the following Schedule RC-C, part I, loan categories:

	RCON	Number of Loans	
a. "Loans secured by farmland (including farm residential and other improvements)" in domestic offices reported in Schedule RC-C, part I, item 1.b, column B	5576. .	N/A	6.a
b. "Loans to finance agricultural production and other loans to farmers" in domestic offices reported in Schedule RC-C, part I, item 3, column B	5577. .	N/A	6.b

Dollar Amounts in Thousands

	RCON	(Column A) Number of Loans	RCON	(Column B) Amount Currently Outstanding	
7. Number and amount currently outstanding of "Loans secured by farmland (including farm residential and other improvements)" in domestic offices reported in Schedule RC-C, part I, item 1.b, column B (sum of items 7.a through 7.c must be less than or equal to Schedule RC-C, part I, item 1.b, column B):					
a. With original amounts of $ 100,000 or less	5578. .	98	5579. .	2,052	7.a
b. With original amounts of more than $100,000 through $ 250,000	5580. .	11	5581. .	1,402	7.b
c. With original amounts of more than $ 250,000 through $ 500,000	5582. .	4	5583. .	1,261	7.c
8. Number and amount currently outstanding of "Loans to finance agricultural production and other loans to farmers" in domestic offices reported in Schedule RC-C, part I, item 3, column B (sum of items 8.a through 8.c must be less than or equal to Schedule RC-C, part I, item 3, column B):					
a. With original amounts of $ 100,000 or less	5584. .	38	5585. .	519	8.a
b. With original amounts of more than $ 100,000 through $ 250,000	5586. .	6	5587. .	608	8.b
c. With original amounts of more than $ 250,000 through $ 500,000	5588. .	2	5589. .	561	8.c

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Schedule RC-D is to be completed only by banks with $1 billion or more in total assets.

Schedule RC-D - Assets Held in Trading Accounts in Domestic Offices Only

C420 <-

	RCON	Dollar Amounts in Thousands	
1. U.S. Treasury securities	1010	N/A	1.
2. U.S. Government agency and corporation obligations	1020	6,495	2.
3. Securities issued by states and political subdivisions in the U.S.	1025	N/A	3.
4. Other bonds, notes, and debentures	1045	N/A	4.
5. Certificates of deposit	1026	N/A	5.
6. Commercial paper	1027	N/A	6.
7. Bankers acceptances	1028	N/A	7.
8. Other	1029	N/A	8.
9. Total (sum of items 1 through 8)	2146	6,495	9.

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Schedule RC-E - Deposit Liabilities

Part I. Deposits in Domestic Offices

C425 <-

Dollar Amounts in Thousands

		Transaction Accounts (Column A) Total transaction accounts (including total demand deposits)		Transaction Accounts (Column B) Memo: Total demand deposits (included in column A)		Nontransaction Accounts (Column C) Total nontransaction accounts (including MMDAs)	
Deposits of:	RCON		RCON		RCON		
1. Individuals, partnerships and corporations	2201..	2,043,230	2240..	1,324,974	2346..	2,451,246	1.
2. U.S. Government	2202..	7,919	2280..	7,919	2520..	0	2.
3. States and political subdivisions in the U.S.	2203..	28,663	2290..	15,226	2530..	15,142	3.
4. Commercial banks in the U.S.	2206..	69,612	2310..	69,612		. . . .	4.
a. U.S. branches and agencies of foreign banks		. . . .		. . . .	2347..	0	4a
b. Other commercial banks in the U.S.		. . . .		. . . .	2348..	693	4b
5. Other depository institutions in the U.S.	2207..	1,166	2312..	1,166	2349..	264	5.
6. Banks in foreign countries	2213..	1,130	2320..	1,130		. . . .	6.
a. Foreign branches of other U.S. banks		. . . .		. . . .	2367..	0	6a
b. Other banks in foreign countries		. . . .		. . . .	2373..	0	6b
7. Foreign governments and official institutions (including foreign central banks)	2216..	0	2300..	0	2377..	0	7.
8. Certified and official checks	2330..	50,674	2330..	50,674		. . . .	8.
9. Total (sum of items 1 through 8) (sum of columns A and C must equal Schedule RC, item 13.a)	2215..	2,202,394	2210..	1,470,701	2385..	2,467,345	9.

Memoranda

Dollar Amounts in Thousands

	RCON		
1. Selected components of total deposits (i.e., sum of item 9, columns A and C):			
a. Total Individual Retirement Accounts (IRAs) and Keogh Plan accounts	6835..	205,732	M.1.a
b. Total brokered deposits	2365..	0	M.1.b
c. Fully insured brokered deposits (included in Memorandum item 1.b above):			
(1) Issued in denominations of less than $ 100,000	2343..	0	M.1.c1
(2) Issued either in denominations of $ 100,000 or in denominations greater than $ 100,000 and participated out by the broker in shares of $ 100,000 or less	2344..	0	M.1.c2
d. Total deposits denominated in foreign currencies	3776..	0	M.1.d
e. Preferred deposits	5590..	27,989	M.1.e
2. Components of total nontransaction accounts (sum of Memoranda items 2.a through 2.d must equal item 9, column C above):			
a. Savings deposits:			
(1) Money market deposit accounts (MMDAs)	6810..	1,286,272	M.2.a1
(2) Other savings deposits (excludes MMDAs)	0352..	238,198	M.2.a2
b. Total time deposits of less than $ 100,000	6648..	758,255	M.2.b
c. Time certificates of deposit of $ 100,000 or more	6645..	184,620	M.2.c
d. Open-account time deposits of $ 100,000 or more	6646..	0	M.2.d
3. All NOW accounts (included in column A above)	2398..	731,693	M.3

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Schedule RC-E - Continued

Part I. Continued

Memoranda (continued)

Deposit Totals for FDIC Insurance Assessments (1)

	RCON	Dollar Amounts in Thousands	
4. Total deposits in domestic offices (sum of item 9, column A and item 9, column C) (must equal Schedule RC, item 13.a)	2200	4,669,739	M.4
a. Total demand deposits (must equal item 9, column B)	2210	1,470,701	M.4.a
b. Total time and savings deposits (2) (must equal item 9, column A plus item 9, column C minus item 9, column B)	2350	3,199,038	M.4.b

(1) An amended Certified Statement should be submitted to the FDIC if the deposit totals reported in this item are amended after the semiannual Certified Statement originally covering this report date has been filed with the FDIC.
(2) For FDIC insurance assessment purposes, "total time and savings deposits" consists of nontransaction accounts and all transaction accounts other than demand deposits.

	RCON	Dollar Amounts in Thousands	
5. Time deposits of less than \$ 100,000 and open-account time deposits of \$ 100,000 or more (included in Memorandum items 2.b and 2.d above) with a remaining maturity or repricing frequency of: (1)			
a. Three months or less	0359	293,139	M.5.a
b. Over three months through 12 months (but not over 12 months)	3644	330,767	M.5.b
6. Maturity and repricing data for time certificates of deposit of \$ 100,000 or more: (1)			
a. Fixed rate time certificates of deposit of \$ 100,000 or more with a remaining maturity of:			
(1) Three months or less	2761	99,806	M.6.a1
(2) Over three months through 12 months	2762	60,186	M.6.a2
(3) Over one year through five years	2763	23,010	M.6.a3
(4) Over five years	2765	0	M.6.a4
(5) Total fixed rate time certificates of deposit of \$ 100,000 or more (sum of Memorandum items 6.a.(1) through 6.a.(4))	2767	183,002	M.6.a5
b. Floating rate time certificates of deposit of \$ 100,000 or more with a repricing frequency of:			
(1) Quarterly or more frequently	4568	1,618	M.6.b1
(2) Annually or more frequently, but less frequently than quarterly	4569	0	M.6.b2
(3) Every five years or more frequently, but less frequently than annually	4571	0	M.6.b3
(4) Less frequently than every five years	4572	0	M.6.b4
(5) Total floating rate time certificates of deposit of \$ 100,000 or more (sum of Memorandum items 6.b.(1) through 6.b.(4))	4573	1,618	M.6.b5
c. Total time certificates of deposit of \$ 100,000 or more (sum of Memorandum items 6.a.(5) and 6.b.(5)) (must equal Memorandum item 2.c above)	6645	184,620	M.6.c

(1) Memorandum items 5 and 6 are not applicable to savings banks that must complete supplemental Schedule RC-J.

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Schedule RC-E - Continued

Part II. Deposits in Foreign Offices (including Edge and Agreement subsidiaries and IBFs)

Deposits of:	RCFN	Dollar Amounts in Thousands	
1. Individuals, partnerships, and corporations	2621	0	1.
2. U.S. banks (including IBFs and foreign branches of U.S. banks)	2623	0	2.
3. Foreign banks (including U.S. branches and agencies of foreign banks, including their IBFs)	2625	0	3.
4. Foreign governments and official institutions (including foreign central banks)	2650	0	4.
5. Certified and official checks	2330	0	5.
6. All other deposits	2668	0	6.
7. Total (sum of items 1 through 6) (must equal Schedule RC, item 13.b)	2200	0	7.

Schedule RC-F - Other Assets

C430 <-

	RCFD	Dollar Amounts in Thousands	
1. Income earned, not collected on loans	2164	13,843	1.
2. Net deferred tax assets (1)	2148	26,997	2.
3. Excess residential mortgage servicing fees receivable	5371	0	3.
4. Other (itemize and describe amounts that exceed 25% of this item)	2168	52,639	4.
TEXT a. 3549: AIR - Investment Securities — RCFD 3549: 18,292			4.a
b. 3550: — 3550: N/A			4.b
c. 3551: — 3551: N/A			4.c
5. Total (sum of items 1 through 4) (must equal Schedule RC, item 11)	2160	93,479	5.

Memorandum

	RCFD	Dollar Amounts in Thousands	
1. Deferred tax assets disallowed for regulatory capital purposes	5610	0	M.1

Schedule RC-G - Other Liabilities

C435 <-

		Dollar Amounts in Thousands	
1. a. Interest accrued and unpaid on deposits in domestic offices (2)	RCON 3645	5,912	1.a
b. Other expenses accrued and unpaid (includes accrued income taxes payable)	RCFD 3646	51,809	1.b
2. Net deferred tax liabilities (1)	3049	0	2.
3. Minority interest in consolidated subsidiaries	3000	0	3.
4. Other (itemize and describe amounts that exceed 25% of this item)	2938	2,126	4.
TEXT a. 3552: Deferred Fee - Unfunded Commitments — RCFD 3552: 1,457			4.a
b. 3553: — 3553: N/A			4.b
c. 3554: — 3554: N/A			4.c
5. Total (sum of items 1 through 4) (must equal Schedule RC, item 20)	2930	59,847	5.

(1) See discussion of deferred income taxes in Glossary entry on "income taxes."

(2) For savings banks, include "dividends" accrued and unpaid on deposits.

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Schedule RC-H - Selected Balance Sheet Items for Domestic Offices

C440 <-

	RCON	Dollar Amounts in Thousands Domestic Offices	
1. Customers' liability to this bank on acceptances outstanding	2155	11,852	1.
2. Bank's liability on acceptances executed and outstanding	2920	11,852	2.
3. Federal funds sold and securities purchased under agreements to resell	1350	156,000	3.
4. Federal funds purchased and securities sold under agreements to repurchase	2800	97,921	4.
5. Other borrowed money	2850	1,085	5.
EITHER			
6. Net due from own foreign offices, Edge and Agreement subsidiaries, and IBFs	2163	N/A	6.
OR			
7. Net due to own foreign offices, Edge and Agreement subsidiaries, and IBFs	2941	0	7.
8. Total assets (excludes net due from foreign offices, Edge and Agreement subsidiaries, and IBFs)	2192	5,364,590	8.
9. Total liabilities (excludes net due to foreign offices, Edge and Agreement subsidiaries, and IBFs)	3129	4,842,723	9.

Memorandum (to be completed only by banks with IBFs and other "foreign" offices)

		Dollar Amounts in Thousands	
EITHER			
1. Net due from the IBF of the domestic offices of the reporting bank	3051	N/A	M.1
OR			
2. Net due to the IBF of the domestic offices of the reporting bank	3059	0	M.2

Schedule RC-I - Selected Assets and Liabilities of IBFs

To be completed only by banks with IBFs and other "foreign" offices.

C445 <-

	RCFN	Dollar Amounts in Thousands	
1. Total IBF assets of the consolidated bank (component of Schedule RC, item 12)	2133	N/A	1.
2. Total IBF loans and lease financing receivables (component of Schedule RC-C, part I, item 12, column A)	2076	N/A	2.
3. IBF commercial and industrial loans (component of Schedule RC-C, part I, item 4, column A)	2077	N/A	3.
4. Total IBF liabilities (component of Schedule RC, item 21)	2898	N/A	4.
5. IBF deposit liabilities due to banks, including other IBFs (component of Schedule RC-E, part II, items 2 and 3)	2379	N/A	5.
6. Other IBF deposit liabilities (component of Schedule RC-E, part II, items 1, 4, 5, and 6)	2381	N/A	6.

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Schedule RC-K - Quarterly Averages (1)

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		Dollar Amounts in Thousands	
ASSETS	RCFD		
1. Interest-bearing balances due from depository institutions	3381	8,187	1.
2. U.S. Treasury securi es and U.S. Government agency and corporation obligations	3382	1,451,111	2.
3. Securities issued by and political subdivisions in the U.S.	3383	878	3.
4. a. Other debt securi es	3647	162,552	4.a
b. Equity securities (includes investments in mutual funds and Federal Reserve stock)	3648	30,754	4.b
5. Federal funds sold and securities purchased under agreements to resell in domestic offices of the bank and of its Edge and Agreement subsidiaries, and in IBFs	3365	128,999	5.
6. Loans:			
a. Loans in domestic offices:	RCON		
(1) Total loans	3360	2,653,125	6.a.1
(2) Loans secured by real estate	3385	836,197	6.a.2
(3) Loans to finance agricultural production and other loans to farmers	3386	1,786	6.a.3
(4) Commercial and industrial loans	3387	1,446,311	6.a.4
(5) Loans to individuals for household, family, and other personal expenditures	3388	263,913	6.a.5
(6) Obligations (other than securities and leases) of states and political subdivisions in the U.S.	3389	93,903	6.a.6
b. Total loans in foreign offices, Edge and Agreement subsidiaries, and IBFs	RCFN 3360	0	6.b
7. Assets held in trading accounts	RCFD 3401	212	7.
8. Lease financing receivables (net of unearned income)	3484	5,580	8.
9. Total assets	3368	5,198,262	9.
LIABILITIES			
10. Interest-bearing transaction accounts in domestic offices (NOW accounts, ATS accounts, and telephone and preauthorized transfer accounts) (exclude demand deposits)	RCON 3485	744,822	10.
11. Nontransaction accounts in domestic offices:			
a. Money market deposit accounts (MMDAs)	3486	1,257,672	11.a
b. Other savings deposits	3487	233,623	11.b
c. ime certificates of deposit of $ 100,000 or more	3345	190,853	11.c
d. All other time deposits	3469	770,987	11.d
12. Interest-bearing deposits in foreign offices, Edge and Agreement subsidiaries, and IBFs	RCFN 3404	0	12.
13. Federal funds purchased and securities sold under agreements to repurchase in domestic offices of the bank and of its Edge and Agreement subsidiaries, and in IBFs	RCFD 3353	58,186	13.
14. Other borrowed money	3355	4,304	14.

(1) For all items, banks have the option of reporting either (1) an average of daily figures for the quarter, or (2) an average of weekly figures (i.e., the Wednesday of each week of the quarter).

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Schedule RC-L - Off-Balance Sheet Items

Please read carefully the instructions for the preparation of Schedule RC-L. Some of the amounts reported in Schedule RC-L are regarded as volume indicators and not necessarily as measures of risk.

C460 <-

	RCFD	Dollar Amounts in Thousands	
1. Unused commitments:			
a. Revolving, open-end lines secured by 1-4 family residential properties, e.g., home equity lines	3814	0	1.a
b. Credit card lines	3815	82,308	1.b
c. Commercial real estate, construction, and land development:			
(1) Commitments to fund loans secured by real estate	3816	56,590	1.c.1
(2) Commitments to fund loans not secured by real estate	6550	18,988	1.c.2
d. Securities underwriting	3817	0	1.d
e. Other unused commitments	3818	1,315,790	1.e
2. Financial standby letters of credit and foreign office guarantees	3819	150,767	2.
a. Amount of financial standby letters of credit conveyed to others — RCFD 3820: 1,032			2.a
3. Performance standby letters of credit and foreign office guarantees	3821	20,450	3.
a. Amount of performance standby letters of credit conveyed to others — RCFD 3822: 107			3.a
4. Commercial and similar letters of credit	3411	110,073	4.
5. Participations in acceptances (as described in the instructions) conveyed to others by the reporting bank	3428	0	5.
6. Participations in acceptances (as described in the instructions) acquired by the reporting (nonaccepting) bank	3429	4,000	6.
7. Securities borrowed	3432	0	7.
8. Securities lent (including customers' securities lent where the customer is indemnified against loss by the reporting bank)	3433	0	8.
9. Mortgages transferred (i.e., sold or swapped) with recourse that have been treated as sold for Call Report purposes:			
a. FNMA and FHLMC residential mortgage loan pools:			
(1) Outstanding principal balance of mortgages transferred as of the report date	3650	0	9.a.1
(2) Amount of recourse exposure on these mortgages as of the report date	3651	0	9.a.2
b. Private (nongovernment-issued or -guaranteed) residential mortgage loan pools:			
(1) Outstanding principal balance of mortgages transferred as of the report date	3652	0	9.b.1
(2) Amount of recourse exposure on these mortgages as of the report date	3653	0	9.b.2
c. Farmer Mac agricultural mortgage loan pools:			
(1) Outstanding principal balance of mortgages transferred as of the report date	3654	0	9.c.1
(2) Amount of recourse exposure on these mortgages as of the report date	3655	0	9.c.2
10. When-issued securities:			
a. Gross commitments to purchase	3434	0	10.a
b. Gross commitments to sell	3435	0	10.b
11. Interest rate contracts (exclude when-issued securities):			
a. Notional value of interest rate swaps	3450	342,151	11.a
b. Futures and forward contracts	3823	0	11.b
c. Option contracts (e.g., options on Treasuries):			
(1) Written option contracts	3824	45,930	11.c.1
(2) Purchased option contracts	3825	45,930	11.c.2
12. Foreign exchange rate contracts:			
a. Notional value of exchange swaps (e.g., cross-currency swaps)	3826	0	12.a
b. Commitments to purchase foreign currencies and U.S. dollar exchange (spot, forward, and futures)	3415	2,192	12.b
c. Option contracts (e.g., options on foreign currency):			
(1) Written option contracts	3827	0	12.c.1
(2) Purchased option contracts	3828	0	12.c.2

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Schedule RC-L - Continued

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		Dollar Amounts in Thousands	
13. Contracts on other commodities and equities:	RCFD		
a. Notional value of other swaps (e.g., oil swaps)	3829	1,135	13.a
b. Futures and forward contracts (e.g., stock index and commodity - precious metals, wheat, cotton, livestock - contracts)	3830	0	13.b
c. Option contracts (e.g., options on commodities, individual stocks and stock indexes):			
(1) Written option contracts	3831	0	13.c1
(2) Purchased option contracts	3832	0	13.c2
14. All other off-balance sheet liabilities (itemize and describe each component of this item over 25% of Schedule RC, item 28, "Total equity capital")	3430	0	14.
TEXT / RCFD			
a. 3555: / 3555 N/A			14.a
b. 3556: / 3556 N/A			14.b
c. 3557: / 3557 N/A			14.c
d. 3558: / 3558 N/A			14.d
15. All other off-balance sheet assets (itemize and describe each component of this item over 25% of Schedule RC, item 28, "Total equity capital")	5591	0	15.
TEXT / RCON			
a. 5592: / 5592 N/A			15.a
b. 5593: / 5593 N/A			15.b
c. 5594: / 5594 N/A			15.c
d. 5595: / 5595 N/A			15.d

Memoranda

		Dollar Amounts in Thousands	
1. Loans originated by the reporting bank that have been sold or participated to others during the calendar quarter ending with the report date (exclude the portions of such loans retained by the reporting bank; see instructions for other exclusions)	RCFD 3431	8,015	M.1
2. Loans purchased by the reporting bank during the calendar quarter ending with the report date (see instructions for exclusions)	3488	13,723	M.2
3. Unused commitments with an original maturity exceeding one year that are reported in Schedule RC-L, items 1.a through 1.e, above (report only the unused portions of commitments that are fee paid or otherwise legally binding)	3833	927,672	M.3
a. Participations in commitments with an original maturity exceeding one year conveyed to others — RCFD 3834 42,915			M.3a
4. To be completed only by banks with $1 billion or more in total assets: Standby letters of credit and foreign office guarantees (both financial and performance) issued to non-U.S. addressees (domicile) included in Schedule RC-L, items 2 and 3, above	3377	731	M.4
5. To be completed for the September report only: Installment loans to individuals for household, family, and other personal expenditures that have been securitized and sold without recourse (with servicing retained), amounts outstanding by type of loan:			
a. Loans to purchase private passenger automobiles	2741	N/A	M.5.a
b. Credit cards and related plans	2742	N/A	M.5.b
c. All other consumer installment credit (including mobile home loans)	2743	N/A	M.5.c

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Schedule RC-M - Memoranda

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		Dollar Amounts in Thousands	
1. Extensions of credit by the reporting bank to its executive officers, directors, principal shareholders, and their related interests as of the report date:			
a. Aggregate amount of all extensions of credit to all executive officers, directors, principal shareholders, and their related interests	RCFD 6164	13,455	1.a
b. Number of executive officers, directors, and principal shareholders to whom the amount of all extensions of credit by the reporting bank (including extensions of credit to related interests) equals or exceeds the lesser of $ 500,000 or 5 percent of total capital as defined for this purpose in agency regulations	RCFD 6165	Number 2	1.b
2. Federal funds sold and securities purchased under agreements to resell with U.S. branches and agencies of foreign banks (1) (included in Schedule RC, items 3.a and 3.b)	3405	0	2.
3. Not applicable.			
4. Outstanding principal balance of 1-4 family residential mortgage loans serviced for others (include both retained servicing and purchased servicing):			
a. Mortgages serviced under a GNMA contract	5500	0	4.a
b. Mortgages serviced under a FHLMC contract:			
(1) Serviced with recourse to servicer	5501	0	4.b.1
(2) Serviced without recourse to servicer	5502	0	4.b.2
c. Mortgages serviced under a FNMA contract:			
(1) Serviced under a regular option contract	5503	0	4.c.1
(2) Serviced under a special option contract	5504	0	4.c.2
d. Mortgages serviced under other servicing contracts	5505	0	4.d
5. To be completed only by banks with $1 billion or more in total assets: Customers' liability to this bank on acceptances outstanding (sum of items 5.a and 5.b must equal Schedule RC, item 9):			
a. U.S. addressees (domicile)	2103	10,506	5.a
b. Non-U.S. addressees (domicile)	2104	1,346	5.b
6. Intangible assets:			
a. Mortgage servicing rights	3164	0	6.a
b. Other identifiable intangible assets:			
(1) Purchased credit card relationships	5506	0	6.b.1
(2) All other identifiable intangible assets	5507	1,312	6.b.2
c. Goodwill	3163	87	6.c
d. Total (sum of items 6.a through 6.c) (must equal Schedule RC, item 10)	2143	1,399	6.d
e. Intangible assets that have been grandfathered for regulatory capital purposes	6442	0	6.e
7. Does your bank have any mandatory convertible debt that is part of your primary or secondary capital?	6167	YES NO X	7.
If yes, complete items 7.a through 7.e:			
a. Total equity contract notes, gross	3290	N/A	7.a
b. Common or perpetual preferred stock dedicated to redeem the above notes	3291	N/A	7.b
c. Total equity commitment notes, gross	3293	N/A	7.c
d. Common or perpetual preferred stock dedicated to redeem the above notes	3294	N/A	7.d
e. Total (item 7.a minus 7.b plus 7.c minus 7.d)	3295	N/A	7.e

(1) Do not report federal funds sold and securities purchased under agreements to resell with other commercial banks in the U.S. in this item.

Schedule RC-M - Continued

		Dollar Amounts in Thousands	
8. a. Other real estate owned:	RCFD		
(1) Direct and indirect investments in real estate ventures	5372. .	0	8.a.1
(2) All other real estate owned:	RCON		
(a) Construction and land development in domestic offices	5508. .	1,380	8.a.2a
(b) Farmland in domestic offices	5509. .	14	8.a.2b
(c) 1-4 family residential properties in domestic offices	5510. .	1,314	8.a.2c
(d) Multifamily (5 or more) residential properties in domestic offices	5511. .	~~26,488~~ -0-	8.a.2d
(e) Nonfarm nonresidential properties in domestic offices	5512. .	26,488 ~~-0-~~ *	8.a.2e
(f) In foreign offices	RCFN 5513. .	0	8.a.2f
(3) Total (sum of items 8.a.(1) and 8.a.(2)) (must equal Schedule RC, item 7)	RCFD 2150. .	29,196	8.a.3
b. Investments in unconsolidated subsidiaries and associated companies:			
(1) Direct and indirect investments in real estate ventures	5374. .	0	8.b.1
(2) All other investments in unconsolidated subsidiaries and associated companies	5375. .	22,019	8.b.2
(3) Total (sum of items 8.b.(1) and 8.b.(2)) (must equal Schedule RC, item 8)	2130. .	22,019	8.b.3
c. Total assets of unconsolidated subsidiaries and associated companies	5376. .	51,333	8.c
9. Noncumulative perpetual preferred stock and related surplus included in Schedule RC, item 23, "Perpetual preferred stock and related surplus"	3778. .	0	9.

Memorandum

		Dollar Amounts in Thousands	
1. Interbank holdings of capital instruments (to be completed for the December report only):			
a. Reciprocal holdings of banking organizations' capital instruments	3836. .	N/A	M.1.a
b. Nonreciprocal holdings of banking organizations' capital instruments	3837. .	N/A	M.1.b

* Nonfarm nonresidential property total was reported in incorrect line item in error. Revised with FDIC Aug. 1993.

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Schedule RC-N - Past Due and Nonaccrual Loans, Leases, and Other Assets

The FFIEC regards the information reported in all of Memorandum item 1, in items 1 through 10, column A, and in Memorandum items 2 and 3, column A, as confidential.

C470 <-

Dollar Amounts in Thousands

	(Column A) Past due 30 through 89 days and still accruing	(Column B) Past due 90 days or more and still accruing		(Column C) Nonaccrual		
1. Loans secured by real estate:	RCFD	RCFD		RCFD		
a. To U.S. addressees (domicile)	1245..	1246..	86	1247..	6,968	1.a
b. To non-U.S. addressees (domicile)	1248..	1249..	0	1250..	0	1.b
2. Loans to depository institutions and acceptances of other banks:						
a. To U.S. banks and other U.S. depository institutions	5377..	5378..	0	5379..	0	2.a
b. To foreign banks	5380..	5381..	0	5382..	0	2.b
3. Loans to finance agricultural production and other loans to farmers	1594..	1597..	0	1583..	29	3.
4. Commercial and industrial loans:						
a. To U.S. addressees (domicile)	1251..	1252..	0	1253..	12,182	4.a
b. To non-U.S. addressees (domicile)	1254..	1255..	0	1256..	0	4.b
5. Loans to individuals for household, family, and other personal expenditures:						
a. Credit cards and related plans	5383..	5384..	2	5385..	0	5.a
b. Other (includes single payment, installment, and all student loans)	5386..	5387..	14	5388..	153	5.b
6. Loans to foreign governments and official institutions	5389..	5390..	0	5391..	0	6.
7. All other loans	5459..	5460..	0	5461..	382	7.
8. Lease financing receivables:						
a. Of U.S. addressees (domicile)	1257..	1258..	0	1259..	0	8.a
b. Of non-U.S. addressees (domicile)	1271..	1272..	0	1791..	0	8.b
9. Debt securities and other assets (exclude other real estate owned and other repossessed assets)	3505..	3506..	0	3507..	0	9.

Amounts reported in items 1 through 8 above include guaranteed and unguaranteed portions of past due and nonaccrual loans and leases. Report in item 10 below certain guaranteed loans and leases that have already been included in the amounts reported in items 1 through 8.

10. Loans and leases reported in items 1 through 8 above which are wholly or partially guaranteed by the U.S. Government	RCFD 5612..	RCFD 5613..	0	RCFD 5614..	0	10.
a. Guaranteed portion of loans and leases included in item 10 above	5615..	5616..	0	5617..	0	10.a

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Schedule RC-N - Continued

Memoranda

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						Dollar Amounts in Thousands	
1. Restructured loans and leases included in Schedule RC-N, items 1 through 8, above	RCFD 1658..		RCFD 1659..		RCFD 1661..		M.1
2. Loans to finance commercial real estate, construction, and land development activities (not secured by real estate) included in Schedule RC-N, items 4 and 7, above	6558..		6559..	0	6560..	106	M.2
3. Loans secured by real estate in domestic offices (included in Schedule RC-N, item 1, above):							
a. Construction and land development	RCON 2759..		RCON 2769..	0	RCON 3492..	1,323	M.3a
b. Secured by farmland	3493..		3494..	14	3495..	82	M.3b
c. Secured by 1-4 family residential properties:							
(1) Revolving, open-end loans secured by 1-4 family residential properties and extended under lines of credit	5398..		5399..	0	5400..	0	M.3c1
(2) All other loans secured by 1-4 family residential properties	5401..		5402..	72	5403..	2,078	M.3c2
d. Secured by multifamily (5 or more) residential properties	3499..		3500..	0	3501..	828	M.3d
e. Secured by nonfarm nonresidential properties	3502..		3503..	0	3504..	2,657	M.3e

Schedule RC-O - Other Data for Deposit Insurance Assessments

An amended Certified Statement should be submitted to the FDIC if the amounts reported in items 1 through 9 of this schedule are amended after the semiannual Certified Statement originally covering this report date has been filed with the FDIC.

C475 <-

		Dollar Amounts in Thousands	
1. Unposted debits (see instructions):	RCON		
a. Actual amount of all unposted debits	0030. .	N/A	1.a
OR			
b. Separate amount of unposted debits:			
(1) Actual amount of unposted debits to demand deposits	0031. .	416	1.b1
(2) Actual amount of unposted debits to time and savings deposits (1)	0032. .	0	1.b2
2. Unposted credits (see instructions):			
a. Actual amount of all unposted credits	3510. .	N/A	2.a
OR			
b. Separate amount of unposted credits:			
(1) Actual amount of unposted credits to demand deposits	3512. .	0	2.b1
(2) Actual amount of unposted credits to time and savings deposits (1)	3514. .	0	2.b2
3. Uninvested trust funds (cash) held in bank's own trust department (not included in total deposits in domestic offices)	3520. .	517	3.
4. Deposits of consolidated subsidiaries in domestic offices and in insured branches in Puerto Rico and U.S. territories and possessions (not included in total deposits):			
a. Demand deposits of consolidated subsidiaries	2211. .	19,221	4.a
b. Time and savings deposits (1) of consolidated subsidiaries	2351. .	0	4.b
c. Interest accrued and unpaid on deposits of consolidated subsidiaries	5514. .	0	4.c
5. Deposits of insured branches in Puerto Rico and U.S. territories and possessions:			
a. Demand deposits in insured branches (included in Schedule RC-E, Part II)	2229. .	0	5.a
b. Time and savings deposits (1) in insured branches (included in Schedule RC-E, Part II)	2383. .	0	5.b
c. Interest accrued and unpaid on deposits in insured branches (included in Schedule RC-G, item 1.b)	5515. .	0	5.c

(1) For FDIC insurance assessment purposes, "time and savings deposits" consists of nontransaction accounts and all transaction accounts other than demand deposits.

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Schedule RC-O - Continued

Dollar Amounts in Thousands

Item 6 is not applicable to state nonmember banks that have not been authorized by the Federal Reserve to act as pass-through correspondents.

6. Reserve balances actually passed through to the Federal Reserve by the reporting bank on behalf of its respondent depository institutions that are also reflected as deposit liabilities of the reporting bank:	RCON			
a. Amount reflected in demand deposits (included in Schedule RC-E, Part I, Memorandum item 4.a)	2314		0	6.a
b. Amount reflected in time and savings deposits (1) (included in Schedule RC-E, Part I, Memorandum item 4.b)	2315		0	6.b
7. Unamortized premiums and discounts on time and savings deposits:(1)				
a. Unamortized premiums	5516		0	7.a
b. Unamortized discounts	5517		0	7.b
8. To be completed by banks with "Oakar deposits." Total "Adjusted Attributable Deposits" of all institutions acquired under Section 5(d)(3) of the Federal Deposit Insurance Act (from most recent FDIC Oakar Transaction Worksheet(s))	5518		795,313	8.
9. Deposits in lifeline accounts	5596			9.

(1) For FDIC insurance assessment purposes, "time and savings deposits" consists of nontransaction accounts and all transaction accounts other than demand deposits.

Memoranda

(to be completed each quarter except as noted) — Dollar Amounts in Thousands

1. Total deposits in domestic offices of the bank (sum of Memorandum items 1.a.(1) and 1.b.(1) must equal Schedule RC, item 13.a):					
a. Deposit accounts of $ 100,000 or less:			RCON		
(1) Amount of deposit accounts of $ 100,000 or less			2702	3,258,804	M.1a1
(2) Number of deposit accounts of $ 100,000 or less (to be completed for the June report only)	RCON 3779	Number 627,915			M.1a2
b. Deposit accounts of more than $ 100,000:					
(1) Amount of deposit accounts of more than $ 100,000			2710	1,410,935	M.1b1
(2) Number of deposit accounts of more than $ 100,000	RCON 2722	Number 3,805			M.1b2

2. Estimated amount of uninsured deposits in domestic offices of the bank:

a. An estimate of your bank's uninsured deposits can be determined by multiplying the number of deposit accounts of more than $ 100,000 reported in Memorandum item 1.b.(2) above by $ 100,000 and subtracting the result from the amount of deposit accounts of more than $ 100,000 reported in Memorandum item 1.b.(1) above.

Indicate in the appropriate box at the right whether your bank has a method or procedure for determining a better estimate of uninsured deposits than the estimate described above	RCON 6861	YES	NO X	M.2.a
b. If the box marked YES has been checked, report the estimate of uninsured deposits determined by using your bank's method or procedure	5597		N/A	M.2.b

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Person to whom questions about the Reports of Condition and Income should be directed:

Dennis Steen, Senior Vice President — (713) 250-7346

Name and Title (TEXT 8901) — Area code and phone number (TEXT 8902)

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Schedule RC-R - Risk-Based Capital

This schedule must be completed by all banks as follows: Banks that reported total assets of $1 billion or more in Schedule RC, item 12, for June 30, 1992, must complete items 2 through 9 and Memorandum item 1. Banks with assets of less than $1 billion must complete items 1 through 3 below or Schedule RC-R in its entirety, depending on their response to item 1 below.

C480 <-

	RCFD	YES	NO	
1. Test for determining the extent to which Schedule RC-R must be completed. To be completed only by banks with total assets of less than $1 billion. Indicate in the appropriate box at the right whether the bank has total capital greater than or equal to eight percent of adjusted total assets	6056	N/A		1.

For purposes of this test, adjusted total assets equals total assets less cash, U.S. Treasuries, U.S. Government agency obligations, and 80 percent of U.S. Government-sponsored agency obligations plus the allowance for loan and lease losses and selected off-balance sheet items as reported on Schedule RC-L (see instructions).

If the box marked YES has been checked, then the bank only has to complete items 2 and 3 below. If the box marked NO has been checked, the bank must complete the remainder of this schedule.

A NO reponse to item 1 does not necessarily mean that the bank's actual risk-based capital ratio is less than eight percent or that the bank is not in compliance with the risk-based capital guidelines.

Dollar Amounts in Thousands

Items 2 and 3 are to be completed by all banks.	RCFD	(Column A) Subordinated Debt (1) and Intermediate Term Preferred Stock	RCFD	(Column B) Other Limited-Life Capital Instruments	
2. Subordinated debt(1) and other limited-life capital instruments (original weighted average maturity of at least five years) with a remaining maturity of:					
a. One year or less	3780	0	3786	0	2.a
b. Over one year through two years	3781	0	3787	0	2.b
c. Over two years through three years	3782	0	3788	0	2.c
d. Over three years through four years	3783	0	3789	0	2.d
e. Over four years through five years	3784	0	3790	0	2.e
f. Over five years	3785	0	3791	0	2.f
3. Total qualifying capital (i.e., Tier 1 and Tier 2 capital) allowable under the risk-based capital guidelines			3792	566,908	3.

Items 4-9 and Memorandum item 1 are to be completed by banks that answered NO to item 1 above and by banks with total assets of $1 billion or more.

	RCFD	(Column A) Assets Recorded on the Balance Sheet	RCFD	(Column B) Credit Equivalent Amount of Off-Balance Sheet Items (2)	
4. Assets and credit equivalent amounts of off-balance sheet items assigned to the Zero percent risk category:					
a. Assets recorded on the balance sheet:					
(1) Securities issued by, other claims on, and claims unconditionally guaranteed by, the U.S. Government and its agencies and other OECD central governments	3794	747,331			4.a.1
(2) All other	3795	160,827			4.a.2
b. Credit equivalent amount of off-balance sheet items			3796	0	4.b

(1) Exclude mandatory convertible debt reported in Schedule RC-M, item 7.e, "Total."

(2) Do not report in column B the risk-weighted amount of assets reported in column A.

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Schedule RC-R - Continued

Dollar Amounts in Thousands

		(Column A) Assets Recorded on the Balance Sheet		(Column B) Credit Equivalent Amount of Off-Balance Sheet Items (1)	
5. Assets and credit equivalent amounts of off-balance sheet items assigned to the 20 percent risk category:					
a. Assets recorded the balance sheet:	RCFD		RCFD		
(1) Claims conditionally guaranteed by the U.S. Government and its agencies and other OECD central governments	3798	48,821			5.a.1
(2) Claims collateralized by securities issued by the U.S. Government and its agencies and other OECD central governments; by securities issued by U.S Government-sponsored agencies; and by cash on deposit	3799	126,280			5.a.2
(3) All other	3800	1,442,446			5.a.3
b. Credi equivalent amount of off-balance sheet items			3801	44,357	5.b
6. Assets and credi equivalent amounts of off-balance sheet items assigned to the 50 percent risk category:					
a. Assets recorded the balance sheet	3802	277,905			6.a
b. Credit equivalent amount of off-balance sheet items			3803	787	6.b
7. Assets and credit equivalent amounts of off-balance sheet tems assigned to the 100 percent risk category:					
a. Assets recorded the balance sheet	3804	2,637,564			7.a
b. Credit equivalent amount of off-balance sheet items			3805	607,312	7.b
8. On-balance sheet values (or portions thereof) of interest rate, foreign exchange rate, and commodity contracts which have capital for thei off-balance sheet exposure under the risk-based capital guidelines and those contracts (e.g., futures contracts) excluded from the calculation of the risk-based capital ratio (exclude margin accounts and accrued receivables from this item)	3806	0			8.
9. Total assets recorded the balance sheet (sum of items 4.a, 5.a, 6.a, 7.a, and 8, column A) (must equal Schedule RC, item 12 plus items 4.b and 4.c, plus Schedule RC-B, item 6.a.(3), column A)	3807	5,441,174			9.

Memorandum

Dollar Amounts in Thousands

		(Column A) Notional Principal Value		(Column B) Replacement Cost (Market Value)	
1. Notional principal value and replacement cost of interest rate and foreign exchange rate contracts in column B, report only those contracts with a positive replacement cost):	RCFD		RCFD		
a. Interest rate contracts (exclude futures contracts)			3808	80	M.1.a
(1) With a remaining maturity of one year or less	3809	93,894			M.1.a1
(2) With a remaining maturity of over one year	3810	294,187			M.1.a2
b. Foreign exchange rate contracts (exclude contracts with an original maturity of 14 days or less and futures contracts)			3811	41	M.1.b
(1) With a remaining maturity of one year or less	3812	2,192			M.1.b1
(2) With a remaining maturity of over one year	3813	N/A			M.1.b2

(1) Do not report in column B the risk-weighted amount of assets reported in column A.

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Optional Narrative Statement Concerning the Amounts Reported in the Reports of Condition and Income

at close of business on June 30, 1993

First Interstate Bank of Texas, NA — Legal Title of Bank
Houston — City
TX — State

The management of the reporting bank may, if it wishes, submit a brief narrative statement on the amounts reported in the Reports of Condition and Income. This optional statement will be made available to the public, along with the publicly available data in the Reports of Condition and Income, in response to any request for individual bank report data. However, the information reported in column A and in all of Memorandum item 1 of Schedule RC-N is regarded as confidential and will not be released to the public. BANKS CHOOSING TO SUBMIT THE NARRATIVE STATEMENT SHOULD ENSURE THAT THE STATEMENT DOES NOT CONTAIN THE NAMES OR OTHER IDENTIFICATIONS OF INDIVIDUAL BANK CUSTOMERS, REFERENCES TO THE AMOUNTS REPORTED IN THE CONFIDENTIAL ITEMS IN SCHEDULE RC-N, OR ANY OTHER INFORMATION THAT THEY ARE NOT WILLING TO HAVE MADE PUBLIC OR THAT WOULD COMPROMISE THE PRIVACY OF THEIR CUSTOMERS. Banks choosing not to make a statement may check the "No comment" box below and should make no entries of any kind in the space provided for the narrative statement; i.e., DO NOT enter in this space such phrases as "No statement," "Not applicable," "N/A," "No comment," and "None."

The optional statement must be entered on this sheet. The statement should not exceed 100 words. Further, regardless of the number of words, the statement must not exceed 750 characters, including punctuation, indentation, and standard spacing between words and sentences. If any submission should exceed 750 characters, as defined, it will be truncated at 750 characters with no notice to the submitting bank and the truncated statement will appear as the bank's statement both on agency computerized records and in computer-file releases to the public.

All information furnished by the bank in the narrative statement must be accurate and not misleading. Appropriate efforts shall be taken by the submitting bank to ensure the statement's accuracy. The statement must be signed, in the space provided below, by a senior officer of the bank who thereby attests to its accuracy.

If, subsequent to the original submission, material changes are submitted for the data reported in the Reports of Condition and Income, the existing narrative statement will be deleted from the files, and from disclosure; the bank, at its option, may replace it with a statement, under signature, appropriate to the amended data.

The optional narrative statement will appear in agency records and in release to the public exactly as submitted (or amended as described in the preceding paragraph) by the management of the bank (except for the truncation of statements exceeding the 750-character limit described above). THE STATEMENT WILL NOT BE EDITED OR SCREENED IN ANY WAY BY THE SUPERVISORY AGENCIES FOR ACCURACY OR RELEVANCE. DISCLOSURE OF THE STATEMENT SHALL NOT SIGNIFY THAT ANY FEDERAL SUPERVISORY AGENCY HAS VERIFIED OR CONFIRMED THE ACCURACY OF THE INFORMATION CONTAINED THEREIN. A STATEMENT TO THIS EFFECT WILL APPEAR ON ANY PUBLIC RELEASE OF THE OPTIONAL STATEMENT SUBMITTED BY THE MANAGEMENT OF THE REPORTING BANK.

C471 C472 <-

No comment: X (RCON 6979)
BANK MANAGEMENT STATEMENT (please type or print clearly) (TEXT 6980):

Signature of Executive Officer of Bank

August 2, 1993 — Date of Signature

First Interstate Bank of Texas, NA
P.O. Box 3326
Houston, TX 77253-3326

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THIS PAGE IS TO BE COMPLETED BY ALL BANKS

OMB No. For OCC:	1557-0081
OMB No. For FDIC:	3064-0052
OMB No. For Federal Reserve:	7100-0036
Expiration Date:	02/28/95

SPECIAL REPORT
(Dollar Amounts in Thousands)

CLOSE OF BUSINESS DATE: June 30, 1993

FDIC Certificate Number: 24344

C700 <-

LOANS TO EXECUTIVE OFFICERS (Complete as of each Call Report Date)

The following information is required by Public Laws 90-44 and 102-242, but does not constitute a part of the Report of Condition. With each Report of Condition, these Laws require all banks to furnish a report of all loans or other extensions of credit to its executive officers made since the date of the previous Report of Condition. Data regarding individual loans or other extensions of credit are not required. If no such loans or other extensions of credit were made during the period, insert "none" against subitem (a). (Exclude the first $ 5,000 of indebtedness of each executive officer under bank credit card plan.) See Sections 215.2 and 215.3 of Title 12 of the Code of Federal Regulations (Federal Reserve Board Regulation O) for the definitions of "executive officer" and "extension of credit," respectively. Exclude loans and other extensions of credit to directors and principal shareholders who are not executive officers.

	RCFD			
a. Number of loans made to executive officers since the previous Call Report date	3561. .		NONE	a.
b. Total dollar amount of above loans (in thousands of dollars)	3562. .		0	b.
c. Range of interest charged on above loans (example: 9-3/4% = 9.75)	7701/7702. .	0.00% to	0.00%	c.

SIGNATURE AND TITLE OF OFFICER AUTHORIZED TO SIGN REPORT

DATE (Month, Day, Year)

August 2, 1993

NAME AND TITLE OF PERSON TO WHOM INQUIRIES MAY BE DIRECTED (TEXT 8903)

Dennis Steen, Senior Vice President

AREA CODE/PHONE NUMBER (TEXT 8904)

(713) 250-7346

FDIC 8040/53 (12-92)

First Interstate Bank of Texas, NA
P.O. Box 3326
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